



6-1-1970

Conglomerate Mergers

Gerald Grieman

Follow this and additional works at: <http://scholarship.law.nd.edu/ndlr>



Part of the [Law Commons](#)

Recommended Citation

Gerald Grieman, *Conglomerate Mergers*, 45 Notre Dame L. Rev. 698 (1970).

Available at: <http://scholarship.law.nd.edu/ndlr/vol45/iss4/6>

This Note is brought to you for free and open access by NDLScholarship. It has been accepted for inclusion in Notre Dame Law Review by an authorized administrator of NDLScholarship. For more information, please contact lawdr@nd.edu.

CONGLOMERATE MERGERS

I. Introduction

One cannot help but wonder how the 1950 amendment of section seven of the Clayton Act¹ would have been worded had the members of Congress been propelled, time-machine-like, into the year 1970, there to see the results of their handiwork. What would they have done had they known that in killing one merger movement they were giving birth to another even more powerful and farreaching—the conglomerate merger mania.

Some, like Attorney General John Mitchell, view the conglomerates with alarm, believing that “the future vitality of our free economy may be in danger because of the increasing threat of economic concentration by corporate mergers.”² Others, like G. William Miller, President of Textron, Inc., a modern conglomerate, see the movement as a boon to competition in that the giants of industry are finally feeling the prod of fresh and vigorous competition. Questions Miller:

Why shouldn't Textron be entitled to test them and see if our innovation, our use of capital, our approach to the market, our willingness to satisfy new human needs can outperform theirs? Why shouldn't we? I feel strongly that Textron should be free to take on the giants.³

Still others argue that even if there is a threat in such concentration, “Congress did not prohibit concentration as such. That an acquisition may increase concentration does not in itself spell illegality.”⁴

Assistant Attorney General Richard McLaren, however, believes that the pace and scale of mergers “can be ignored only at the risk of serious and irreversible damage to our economy.”⁵ As a result, McLaren is “willing to risk losing some cases to find out” how far the present powers will go in “halting the current accelerated trend toward concentration by merger and—as I see it—the severe economic and social dislocations” which accompany it.⁶ In testing his theory of section seven, McLaren has filed suit to block merger plans of three leading conglomerates: Ling-Temco-Vought (Jones & Laughlin Steel Corp.),⁷ International Telephone & Telegraph (Hartford Fire Insurance Company, Canteen Corporation, and Grinnell Corporation),⁸ and Northwest Industries (B.F. Goodrich Co.).⁹

1 Celler-Kefauver Act of 1950, 15 U.S.C. § 18 (1964).

2 *Address of John N. Mitchell*, 6 GA. ST. B.J. 92 (1969).

3 U.S. NEWS & WORLD REP., Oct. 28, 1968, at 79.

4 Handler & Robinson, *A Decade of Administration of the Celler-Kefauver Antimerger Act*, in 2 M. HOFFMANN & A. WINARD, *HOFFMANN'S ANTITRUST LAW AND TECHNIQUES* 303, 362 (1963).

5 AMERICA, June 14, 1969, at 683.

6 U.S. NEWS & WORLD REP., Mar. 24, 1969, at 87.

7 *United States v. Ling-Temco-Vought, Inc.*, Civil No. 69-438 (W.D. Pa., filed April 14, 1969).

8 *United States v. International Tel. & Tel. Corp.*, Civil No. 69C-924 (N.D. Ill. 1968); *United States v. International Tel. & Tel. Corp.*, Civil No. 13320 (D. Conn., filed Aug. 1, 1969), *prelim. inj. denied*, 1969 Trade Cas. ¶ 72,943; *United States v. International Tel. & Tel. Corp.*, Civil No. 13319 (D. Conn., filed Aug. 1, 1969), *prelim. inj. denied*, 1969 Trade Cas. ¶ 72,943.

9 *United States v. Northwest Indus., Inc.*, Civil No. 69C-1102 (N.D. Ill., filed May 21, 1969), *prelim. inj. denied*, 1969 Trade Cas. ¶ 72,853.

Conglomerate, never an easy word to define, has become even more slippery now that it is "considered a polysyllabic dirty word."¹⁰ Today, a company describes itself as "diversified" or "multi-industry"; it recoils from being labeled "conglomerate." Since there is even less precision in the new terminology than in the old, there is no reason to depart from the traditional classifications. A horizontal merger is defined as a combination of two companies that sell the same product within the same market.¹¹ A vertical merger occurs when a manufacturer combines with his distributor, customer, or supplier. Any other type of merger will be called a conglomerate merger.

The broad conglomerate classification may be divided into three subgroups. In the first type, product extension, a company will merely complete its product line; the new product is related to, but not identical with the old. The second, market extension, is a combination of two companies that sell the same product in different sections of the country. In the pure conglomerate merger, the last subgroup, there is no connection between the products of the acquiring and acquired firms.

The conglomerate company is not a radical innovation in American business; it is, rather, a concept that has lain dormant since the conglomerates of another age were formed—General Electric, General Motors, Procter & Gamble. The new conglomerateers, like Textron's Miller, argue that only a new breed of equally large companies will be able to increase competition by challenging these established giants. Miller asks, "Are we going to be permitted to challenge them in the marketplace? Are we going to be allowed to reach the size we need to compete with these companies? Are we going to let only the companies that have become big remain big?"¹²

Surprisingly, President Nixon's Task Force on Productivity and Competition (the Stigler Report) supported this viewpoint and failed to back the Justice Department. In its report, the task force expressed serious doubt "that the Anti-trust Division should embark upon an active program of challenging conglomerate enterprises on the basis of nebulous fears about size and economic power."¹³

Many of the new breed have ventured into farther-flung areas than the old conglomerateers had dared. "In the modern conglomerate, oil and water do mix. So do steel and airlines, theaters and tobacco, chemicals and clothes, meat-packing and insurance."¹⁴ Charles G. Bludhorn, Chairman of Gulf & Western, the most active of the new conglomerates, explains the new phenomenon in a homely way: "If you have all your eggs in one basket, you're stuck with those eggs. But if you've also got apples and bananas, that's something else."¹⁵ Some of the less venturesome of the new conglomerateers have been more cautious in filling their baskets. Willard F. Rockwell, Chairman of North American Rockwell is

10 BUS. WEEK, Aug. 2, 1969, at 27.

11 While a market-extension merger could often be classified as a horizontal merger in that the merger helps in attaining a dominant position with regard to a single product, it will be included in the conglomerate class for the purpose of this paper.

12 U.S. NEWS & WORLD REP., Oct. 28, 1968, at 79.

13 *Report of the Task Force on Productivity and Competition*, 2 ANTITRUST L. & ECON. REV., Spring, 1969, at 13, 31 [hereinafter cited as STIGLER REPORT].

14 TIME, Mar. 7, 1969, at 75.

15 TIME, July 19, 1968, at 64.

very skeptical of a corporate mixture where you throw together under one management many different kinds of unrelated businesses—for example, an insurance company, a manufacturing company, a food processor, a shipyard

I think it is basically unhealthy.

Such corporations are headed for trouble in anything other than a continually rising economy. Just because an executive is good at running a manufacturing concern doesn't mean he can take over the operations of a bank or an insurance company.¹⁶

The differing attitudes are reflected in the product mix of the companies of these two men; North American Rockwell restricts itself to dealings in highly engineered items such as aircraft, machine tools, textile machinery, and auto parts, while Gulf & Western has dabbled in such diverse, unrelated fields as agriculture, mining, entertainment, real estate, auto parts, and publishing, to name only a few.

Even the relatively conservative Rockwell does not go far enough to suit McLaren, who believes there is just too much business going into too few baskets. The Justice Department argues that

[i]n the last twenty years, an accelerating merger movement in the United States has substantially increased aggregate concentration and eliminated the independent existence of a rising number of very large firms. This trend has reduced the number of firms likely to enter many of the nation's concentrated industries, the number of sources of competitive innovation, and the centers of decision making upon important industrial and commercial matters. To an increasing extent these mergers have involved large firms which rank among the leading firms in concentrated markets.¹⁷

The record is, indeed, disturbing. During the last two years conglomerates have swallowed up Jones & Laughlin Steel, Lorillard, Wilson, United Fruit, Armour, and the Boston Celtics. Whispers have even been heard about possible attacks on giants such as A&P, Pan American, and U. S. Steel!¹⁸ McLaren noted that "[i]t was the accelerating trend of these very large mergers—which seemed to be announced with greater and greater frequency during 1968 and in early 1969—that gave us particular concern."¹⁹

The post-World War II merger boom, which sparked the 1950 Celler-Kefauver amendment of section seven of the Clayton Act, ended with the 200 largest companies controlling 48.1 percent of total manufacturing assets in 1948.²⁰ At the peak of this merger cycle, there were over 400 manufacturing and mining mergers per year;²¹ by 1949, merger activity had reached a postwar low.²² Most of the mergers of this period were either horizontal or vertical; from 1948 to

16 U.S. NEWS & WORLD REP., May 19, 1969, at 71-72.

17 Complaint at 7, *United States v. International Tel. & Tel. Corp.*, Civil No. 13320 (D. Conn. filed Aug. 1, 1969).

18 TIME, Mar. 7, 1969, at 76.

19 *Hearings on Public Policies Toward Conglomerate Mergers Before the Senate Subcomm. on Antitrust and Monopoly of the Comm. on the Judiciary*, 91st Cong., 1st Sess. (1970) (testimony of Richard W. McLaren) [hereinafter cited as *1970 Hearings*].

20 STUDIES BY THE STAFF OF THE CABINET COMMITTEE ON PRICE STABILITY 79 (1969) [hereinafter cited as *CABINET COMMITTEE STUDIES*].

21 *Id.* at 72.

22 *Id.*

1951, conglomerate mergers accounted for only 38.1 percent of all mergers.²³

In 1954, the merger boom began anew and still continues today.²⁴ From 1955 to 1965, the number of mining and manufacturing firms acquired per year ranged from 700 to 1000—double the rate of the postwar era; by 1968, the number reached nearly 3000 mergers per year, nearly seven and one-half times that of the postwar movement!²⁵ Further, a change had been detected in the types of merger carried out; in 1968, 91 percent of all mergers were of the conglomerate variety.²⁶ The Cabinet Committee on Price Stability also noted a change in aggregate concentration:

By 1967, the 100 largest corporations held 47.6 percent, and the 200 largest corporations held 58.7 percent of the assets of all manufacturing corporations. By 1967 the 100 largest manufacturing corporations held about the same share of assets held by the 200 largest in 1948.

... [T]he 529 corporations with assets of \$100 million or more held 73 percent.²⁷

Harold S. Geneen, President of International Telephone & Telegraph, argues that these figures are misleading. He contends that 1948 is an improper base year "because it is one of the lowest points in the cycle of available information. . . . [I]f one goes back to 1932, one will get a different trend. The concentration in the top 140 companies since 1932 was not different than in 1963!"²⁸ Geneen's argument, however, overlooks the point of the statistics, i.e., that the current merger boom is causing a great increase in the amount of aggregate concentration; 1948 is an appropriate starting point precisely *because* it shows the effect of the boom unmodified by a decline that may have occurred from 1932 to 1948.

Former Assistant Attorney General Donald Turner has also refused to become alarmed at the rising tide of concentration because "[a]lmost any way that one defines 'small business,' their absolute number has risen steadily and substantially over the years, and the relative number of small firms to large ones appears to have remained remarkably stable."²⁹ Turner, however, overlooks one

23 *Address of John N. Mitchell, supra* note 2, at 94.

24 With the bringing of the antitrust suits in the conglomerate cases cited above, merger activity slowed somewhat. For 1969, the total dipped slightly for the first time in six years. In 1969, for example, there were 160 mergers involving companies with combined assets of \$10 million, compared to 201 in 1968. *U.S. News & World Rep.*, Feb. 23, 1970, at 74. While the number of very large mergers has declined somewhat, McLaren points out that "merger activity generally continues at near-record levels." *1970 Hearings*. James Nicholson points out that, even with the slight slowdown, 1969 was still "the year of the greatest merger activity in history." *Id.* He also notes the timing of the activity:

Acquisitions of companies of over \$10 million of assets were higher during the first quarter of calendar 1969 than the corresponding quarter of 1968, declined slightly relative to 1968, during the second and third quarters of 1969, then increased again during the fourth quarter. *Id.* (emphasis added).

The boom, then, has clearly not ended.

25 CABINET COMMITTEE STUDIES 71. The Cabinet Committee predicted 2300 mergers for 1968 based on eleven months. Willard F. Mueller, FTC economist, set the figure at 2930. *U.S. News & World Rep.*, Mar. 24, 1969, at 86.

26 *Address of John N. Mitchell, supra* note 2, at 94.

27 CABINET COMMITTEE STUDIES 45.

28 Geneen, *A Businessman's View*, 25 *BUS. LAW.* 559, 564 (1970).

29 Turner, *Conglomerate Mergers and Section 7 of the Clayton Act*, 78 *HARV. L. REV.* 1313, 1327 (1965).

very basic fact: a twelve-year-old's lemonade stand can hardly offer the type of competition that will worry the executives of Sunkist. The Cabinet Committee, however, pointed out that "[a]lthough about 250,000 proprietorships and partnerships are engaged in some form of manufacturing, their assets are less than 2 percent of the assets of manufacturing corporations."³⁰ With a rise in the absolute number of small businesses, their relative market position has grown still worse, as an increasing number of companies must share a decreasing percentage of the total business.

It is further revealing to look at the size of the acquired firms. Caspar W. Weinberger, Chairman of the FTC, points out that it is "the viable medium tier [of companies]—which we would expect to grow in the normal way and thereafter present a real competitive challenge to the top companies."³¹ As a result, even the truly large companies are no longer safe: "[f]rom 1948 to 1966, only five firms with assets of over \$250 million were acquired; in 1967 alone, six such firms disappeared via acquisitions; and in 1968, the number rose to 12."³² One firm (Hartford Fire Insurance Company) had assets of nearly \$2 billion,³³ while another (Jones & Laughlin Steel) topped \$1 billion.³⁴ Smaller firms with assets of more than \$25 million fared even worse: "At the beginning of 1968, there were about 1,300 firms with assets of over \$25 million. Had it not been for acquisitions during the past decade, these firms would now number well over 1,900."³⁵

It was the firms with \$10-25 million in assets, however, that fared the worst. The Cabinet Committee found that

the 593 acquired companies [acquired between 1948 and 1967] with assets between \$10 million and \$25 million at time of acquisition were equal to 52 percent of the total number and 50 percent of the total assets of all companies of this size operating in 1967.³⁶

When dealing in long-range figures, it is important to note, the figures represent a minimum estimate of the total effect on market distribution, since merger figures measure only immediate impact; the figures are not adjusted to show how the company would have grown had the acquisition not taken place.

The Cabinet Committee concluded that companies with assets in excess of \$10 million were greatly affected by the merger wave and that "[h]ad these companies not been acquired, had they continued as independent businesses, there would have been at least 40 percent more companies with assets of \$10 million or more operating in 1967."³⁷

30 CABINET COMMITTEE STUDIES 45.

31 1970 *Hearings* (testimony of Caspar W. Weinberger).

32 *Address of John N. Mitchell*, *supra* note 2, at 93.

33 STAFF OF FEDERAL TRADE COMMISSION, ECONOMIC REPORT ON CORPORATE MERGERS, in *Hearings on Economic Concentration Before the Senate Subcomm. on Antitrust and Monopoly of the Comm. on the Judiciary*, 91st Cong., 1st Sess., pt. 8A, at 542 (1969) [hereinafter cited as FTC REPORT].

34 *Id.* at 517.

35 *Address of John N. Mitchell*, *supra* note 2, at 92.

36 CABINET COMMITTEE STUDIES 75.

37 *Id.* An unknown, though perhaps large, number of companies would have entered the \$10 million class by 1967 had they not been acquired. Very few of these companies were failing concerns which would have declined had the merger not occurred. *Id.*

The figures for 1968 show the movement accelerating even faster. In that year, 192 large firms with total assets of \$12.6 billion,³⁸ and individual "assets of 10 million dollars or more, were gobbled up by other large firms. This means that in one year, about 8 percent of all manufacturers of this size surrendered their independence through the merger process."³⁹ Nearly 40 percent of these large firms were acquired by firms ranking in the top 200.⁴⁰

Perhaps the most important effect of the current merger movement is the tremendous reduction in the number of medium-sized firms in the economy. The individual proprietorships and partnerships are not real threats to the giants; the "actual or potential rivals of the top 200 companies come from a relatively small group of medium sized firms with assets between about \$25 million and \$250 million. At the end of 1967, the 1,048 companies of this size accounted for about 17 percent of all manufacturing assets."⁴¹ It is precisely these companies, however, that are being swallowed up by the giant firms. In 1959, there were 883 firms with assets of more than \$25 million.⁴² When projected at the rate of growth of the previous twenty-year period, the figure would grow to 1,970 by 1968.⁴³ Instead, the total number of firms reached only 1,320; mergers accounted for most of the difference.⁴⁴ Although an increase of 200 was projected for 1967, the number remained virtually static due to the merger drain.⁴⁵

Not only are the top firms rapidly devouring their smaller competition, but they also

increasingly occupy positions of leadership in their industries. . . . [I]n 1958, 29 companies [of the top 100 manufacturing firms] were among the 4 leaders in 4 or more industries; by 1963 there were 48 such companies. On the other hand, in 1958 five companies were leaders in no industries and 18 were among the leaders in only one industry. By 1963, there were no companies that were not among the leaders in at least one industry and only seven companies were leaders in only one industry.⁴⁶

It is evident, then, that along with the increase in aggregate concentration the top firms have also greatly expanded their power base.

Furthermore, many of the large, diversified firms have become "partially integrated through a vast network of jointly owned subsidiary companies."⁴⁷ These interlocking directorates have further prejudiced the decision-making process. The process is further muddled when banking trust departments or bank conglomerates enter the picture.

It is, then, understandable why the Department of Justice is concerned about these "nationwide marketing, managerial and financial structures whose

38 U.S. NEWS & WORLD REP., Mar. 24, 1969, at 86.

39 U.S. NEWS & WORLD REP., Feb. 24, 1969, at 86.

40 Address of John N. Mitchell, *supra* note 2, at 93. This amounted to 74 of the 192 firms acquired.

41 CABINET COMMITTEE STUDIES 80.

42 *Id.*

43 *Id.*

44 *Id.*

45 *Id.* at 81.

46 *Id.* at 49.

47 *Id.* at 82.

enormous physical and psychological resources pose substantial barriers to smaller firms wishing to participate in a competitive market."⁴⁸

Other questions, however, remain. Does public policy demand such mergers; is their utility so great that their benefits outweigh any accompanying harm? Does section seven as traditionally understood prohibit such mergers? Can section seven also be interpreted to forbid mergers that greatly increase aggregate concentration?

Since these questions will be examined in the context of the recent antitrust suits brought by the Department of Justice, it is appropriate that the companies involved be examined more closely.

II. The Parties

As stated previously, there is no archetype conglomerate. A firm may, like North American Rockwell, remain within one general area; it may also, like Gulf & Western, branch into highly divergent, unrelated fields.

Management structure also varies widely among the new conglomerates. One may operate on the order of a confederation, with each of the component firms exercising a great deal of sovereignty, while another may choose to have a central management directly controlling the day-to-day operations of every component firm. ITT President Geneen sees the difference as

[w]hether they provide within the parent company a broad group of central management skills, applicable not only to the overall corporate areas such as financing, legal, and stockholder relations, but also to the *operating areas* of the company.⁴⁹

Another major difference among the new conglomerates is the manner in which new firms are acquired. While many takeovers are accomplished by peaceful negotiations between all parties involved, others are effected by hostile tenders or raids that leave the target company a broken hulk. McLaren tells of an executive of a conglomerate-swallowed company: "Wrote the executive to a friend: 'You ask me what it's like to work for a conglomerate? Well, it's just like being a mushroom. First, they keep you in the dark for months. Then they throw dung all over you. Then they can you.'"⁵⁰

Although all three firms in the Justice Department suits are all multi-industry firms, they otherwise run the gamut of differences. Because of these variations, the cases should eventually establish guidelines for all conglomerate mergers.

A. Ling-Temco-Vought

In April, 1969, for the fourth time in ten years, the Justice Department decided to file suit to block a merger involving Dallas-based conglomerate Ling-Temco-Vought.⁵¹ This time, the object was to order LTV to divest itself of its

48 *Address of John N. Mitchell, supra* note 2, at 93.

49 Geneen, *supra* note 28, at 561.

50 TIME, May 23, 1969, at 100.

51 *United States v. Ling-Temco Electronics, Inc.*, 1961 Trade Cas. ¶ 78,621 (N.D. Tex. 1961); *United States v. Wilson Sporting Goods Co.*, 288 F. Supp. 543 (N.D. Ill. 1968); *United States v. Ling-Temco-Vought, Inc.*, Civil No. 69-438 (W.D. Pa., filed April 14, 1969).

eighty-one percent interest in mammoth Jones & Laughlin Steel Corporation, the nation's sixth largest steelmaker. The move caught LTV by surprise since Donald Turner, former Assistant Attorney General, had seemed to indicate that the Department of Justice would have no objection to the merger.⁵² James Ling, LTV's Chairman of the Board and Chief Executive Officer, angrily denounced the suit as "tainted and suspect."⁵³

In thirteen years, Ling's machinations have transformed his tiny electrical contracting firm into a multi-billion-dollar confederation-style conglomerate that ranks as the twenty-second largest industrial company in the nation.⁵⁴ Under Ling's theory of conglomerate business, the subsidiaries, although tied to the parent company, exercise a great deal of autonomy. Each company is responsible for its own operations; Ling says: "When the subsidiaries are paying for their own services rather than the parent, they are more likely to think twice about spending money."⁵⁵ Accordingly, LTV's corporate staff was recently trimmed by 35 percent, from 318 to 205.⁵⁶ Ling still, however, refuses to call LTV a holding company, insisting that it is merely decentralized; the "control emphasis [is] at the subsidiary directorate and executive committee levels, with several parent executives keeping close watch as professional directors."⁵⁷

In 1961, with the merger of Ling-Temco, a small electronics and subcontracting firm, and Chance Vought, a small military aircraft manufacturer, LTV began its climb to the top. In August, 1961, the Justice Department filed suit to block the merger of the two relatively small companies,⁵⁸ but LTV won the "unbelievable lawsuit" within four months of the initial filing date.⁵⁹ At this time, LTV was relatively specialized, with 90 percent of its sales being made to the government.⁶⁰ After suffering severe contract cancellations, Ling vowed "that our company never again would be dependent on one product, one technology, or one customer."⁶¹

In 1964, Washington urged defense contractors to diversify; LTV responded by acquiring the Okonite Corporation, a wire and cable producer, from the Kennecott Copper Corporation, which was disposing of it due to previous antitrust problems. Again the merger was challenged, but the courts refused to restrain it.

In 1967, LTV took a major step in its diversification program by purchasing Wilson & Co. In line with its "Project Redeployment" policy,⁶² LTV split Wilson into three separate publicly owned companies — Wilson Sporting Goods Company (which it sold in mid-1969 to PepsiCo Inc.), Wilson Pharmaceutical &

Suit was also brought in 1965 to block LTV's acquisition of Okonite Corporation. Ling, *The Conglomerate and Antitrust*, 25 BUS. LAW. 571, 574 (1970).

52 Ling, *supra* note 51, at 576.

53 *Id.*

54 1970 Hearings (testimony of Dr. John M. Blair).

55 BUS. WEEK, Aug. 23, 1969, at 27.

56 *Id.*

57 *Id.*

58 *United States v. Ling-Temco Electronics, Inc.*, 1961 Trade Cas. ¶ 78,621 (N.D. Tex. 1961).

59 115 CONG. REC. E7071 (daily ed. Sept. 3, 1969).

60 Ling, *supra* note 51, at 571.

61 *Id.*

62 "Project Redeployment" is a process whereby LTV operating divisions, upon attaining a certain size, are spun off into publicly owned LTV satellites.

Chemical Corporation, and Wilson & Co. (now further redeployed), which retained only the meat and food-processing divisions.⁶³ By the end of 1968, the Wilson trio showed sales of over \$1 billion, with profits in excess of \$17.5 million, representing respective increases of 30 percent and 95 percent over comparable figures for 1965.⁶⁴ Flushed with triumph, LTV rapidly acquired Great-America, essentially Braniff Airways and National Car Rental (which it later sold in mid-1969), and prepared the friendly assault on sluggish, troubled Jones & Laughlin.⁶⁵ In bringing about the largest conglomerate merger in history,⁶⁶ Ling demonstrated the financial wizardry that had propelled LTV to the top; his triumph, however, was short-lived. With the coming of the antitrust suit, Ling found himself with nearly half his assets (about \$400 million) tied up in a sagging company that he was forbidden by court order to manage.⁶⁷ For the first half of 1969, LTV was faced with a net loss of \$679,000, compared to \$19.2 million earned a year earlier.⁶⁸ By the end of the year, operating profits showed a 90 percent drop and a net loss of \$8.3 million after the deduction of an extraordinary charge.⁶⁹

Faced with this unhappy picture, Ling had three alternatives: (1) divest his interest in J&L, which one observer had referred to as "an albatross weighing down the previously fast-moving Dallas conglomerate";⁷⁰ (2) ride out a suit that might last from three to five years while continuing to pay an effective interest rate of eleven percent on the money borrowed to finance the J&L acquisition,⁷¹ an investment in which it could play no managerial role; or (3) settle out of court. Ling chose the settlement and on March 10, 1970, tentatively agreed to a consent decree that ordered what Attorney General Mitchell called "the most substantial corporate divestiture of any antitrust decree in recent years."⁷²

The decree calls for a divestiture of LTV's interest in Braniff and Okonite, forbids LTV from acquiring any company with assets of \$100 million or more for the next ten years, and orders extensive procedures designed to rid LTV of any vestige of reciprocal trading. While Ling sees the restrictions as "somewhat restrictive," he also finds "considerable latitude in terms of possible future opportunities where acquisitions are feasible and otherwise indicated for the company's diversified growth."⁷³ One observer saw the consent decree as a coup

63 The already redeployed Wilson & Co. is now the subject of a second redeployment program. In September, 1969, Ling announced a plan to reorganize Wilson into a parent and five subsidiary companies, with four of the five subsidiaries offering stock to the public. *BUS. WEEK*, Sept. 13, 1969, at 51.

64 Ling, *supra* note 51, at 573. The validity of these figures as indicators of the company's true financial position has been questioned. See Briloff, *Accounting Practices and the Merger Movement*, 45 *NOTRE DAME LAWYER* 604 (1970).

65 While J&L management did not publicly support the merger (had they advised the stockholders to accept the offer, they might have been subject to a lawsuit if the stock rose above the exchange price of \$62.50 per share), all tendered their securities in the first go-round. *FORTUNE*, Sept., 1969, at 136.

66 *TIME*, Apr. 4, 1969, at 89. It will, however, be topped by the ITT-Hartford merger.

67 *FORTUNE*, Sept., 1969 at 136.

68 *BUS. WEEK*, Aug. 23, 1969, at 27.

69 *The Wall Street Journal*, Feb. 19, 1970, at 4, col. 3.

70 *The Wall Street Journal*, Jan. 5, 1970, at 1, col. 6.

71 *The Wall Street Journal*, Mar. 9, 1970, at 28, col. 2.

72 *Id.* col. 1.

73 *Id.*

for LTV: "Ling-Temco will have solved a lawsuit, be well on its way to curing its financial ills and still have up to 95 percent of its earnings power left after getting rid of some problem companies."⁷⁴ Now, with the preliminary injunction dissolved, Ling is free to tackle the dismal situation at J&L; the task will not be an easy one.

B. Northwest Industries

The attempted takeover of the B. F. Goodrich Company by Northwest Industries, Inc., was hardly as amicable as the LTV-J&L merger. Goodrich's tactics, especially an outlandish bank credit agreement, were so extreme that Judge Hubert L. Will, in shocked disbelief, likened the agreement to a "Herman Goering cyanide pill under which it threatened to commit financial suicide in the event that this transaction is consummated. It's a shocking document. It's the worst indictment of Goodrich management of anything in the record in this case."⁷⁵

Ben Heineman, President of Northwest Industries, had been famed as the wonder boy who took over the dying Chicago & Northwestern Railway in 1956 and not only made the commuter trains run at a profit but, more miraculously, on time.

He enlarged the railroad operations by acquiring the Milwaukee Road, a combination that gave the Northwest Lines the "largest railroad in miles of track operated and the sixth largest railroad in gross total operating revenues."⁷⁶ In 1967, he formed a holding company called Northwest Industries, Inc., and soon acquired Philadelphia & Reading Corp., an early conglomerate built on an old anthracite business, which owned such diverse companies as Lone Star Steel, Fruit of the Loom, Inc., and Universal Manufacturing Corporation. Its products ranged from boots and underwear to insulated wire and fluorescent ballasts. Subsidiaries Velsicol Chemical Corporation and Michigan Chemical Corporation further diversified his holdings. Sales rose impressively, from \$260 million in 1965 to \$701 million in 1968.⁷⁷

To the ambitious Heineman, Goodrich looked like a perfect complement to his empire; its product mix would fit in well with Northwest's present blend, but, more important, conservative management had netted Goodrich only 3.9 percent on \$1.1 billion in sales, the lowest profit margin among the Big Four.⁷⁸ Furthermore, shares were widely scattered and relatively cheap, a perfect set-up for a raid.

Goodrich, unwilling to lose its independence, fought back viciously, waging an all-out fight against the raider.⁷⁹ It immediately bought Gulf Oil's one-half

⁷⁴ *Id.* col. 3.

⁷⁵ *FORTUNE*, July, 1969, at 189.

⁷⁶ Brief in Support of Plaintiff's Motion for Preliminary Injunction at 14, *United States v. Northwest Indus., Inc.*, Civil No. 69C-1102 (N.D. Ill., filed May 21, 1969), *prelim. inj. denied*, 1969 Trade Cas. ¶ 72,853 (N.D. Ill. 1969). The new Burlington Northern will operate 24,398 miles of track. *Chicago Sun-Times*, Mar. 3, 1970, at 20.

⁷⁷ *TIME*, May 23, 1969, at 98.

⁷⁸ *Id.* Of the other members of the Big Four, Goodyear has a 5.1 percent return, Uniroyal 4 percent, and Firestone 6 percent.

⁷⁹ For a general discussion of Goodrich's maneuvers see *FORTUNE*, July, 1969, at 110; *FORBES*, Apr. 15, 1969, at 46.

interest in Goodrich-Gulf, a money losing joint venture; this put 5 percent of Goodrich stock in friendly hands. Six weeks later, in a frantic attempt to involve the Interstate Commerce Commission, Goodrich acquired Motor Freight Corp., a trucking firm that closely duplicated the route of the Chicago & Northwestern. When Northwest's stock began to dip, Goodrich notified its stockholders by letter and newspaper ads. It staggered the terms of its directors so that Northwest could not get immediate control even if the tender succeeded. The Ohio Attorney General barred Northwest from offering the stock deal anywhere in Ohio, the home state of the firm. When the government announced its antitrust objections to the merger, Heineman sneered: "There are a lot of frightened, stodgy companies with frightened, stodgy managements. Conservative businessmen are running to the Government saying, 'Save me, save me,' and very often it is at the expense of stockholders."⁸⁰

With stock values plummeting, earnings for the first six months of 1969 down to \$1,502,000 from \$32,934,000 in 1968,⁸¹ and a court battle over the antitrust aspects of the proposed Goodrich takeover, Heineman doggedly pushes on.

C. International Telephone & Telegraph

Unlike LTV, which began as a miniscule electrical company, and Northwest Industries, which grew out of a dying railroad, International Telephone & Telegraph Corporation was already a very large company before it began its program of conglomerate acquisitions. ITT is a "vast international organization, which 'is constantly at work around the clock — in 67 nations on 6 continents,' in activities extending 'from the Arctic to the Antarctic and quite literally from the bottom of the sea to the moon.'"⁸²

ITT also differs in its managerial system; it "operates on the basis of a coherent operating company with a substantial central operating management," having "2,000 industrial and operational specialists in [its] central management group."⁸³ Like LTV, ITT's mergers have been friendly; Geneen proudly boasts: "We have not had to make hostile tenders, and we have had no disagreements on values by the Boards and the stockholders of such companies."⁸⁴

Since ITT began its diversification program in 1960, it has been the third most acquisitive firm in the nation in terms of aggregate assets acquired, purchasing forty-seven companies with aggregate assets of almost \$1.5 billion.⁸⁵ ITT followed a pattern similar to that of LTV, expanding first by acquiring companies technologically related to its field, telecommunications, and only later expanding into unrelated fields. By 1968, ITT owned such diverse companies as Sheraton Corp. of America, an international hotel system, Aetna Finance Co., Continental Baking Co., the nation's largest bread and cake baking company, Levitt & Sons, Inc., the leader in residential construction, and Avis

80 TIME, May 23, 1969, at 100.

81 NEWSWEEK, Aug. 25, 1969, at 58.

82 FTC REPORT 523 citing 1968 ITT Annual Report 7.

83 Geneen, *supra* note 28, at 561.

84 *Id.* at 563.

85 FTC REPORT 26.

Car Rental. With assets of \$4 billion, ITT ranked fifteenth among U.S. manufacturers and was among the top twenty industrials worldwide.⁸⁶

In 1969, ITT acquired Hartford Fire Insurance Co., Grinnell Corporation, and Canteen Corporation (vending food services), companies with total assets of \$2 billion;⁸⁷ this was more than enough to vault past Gulf & Western and LTV, which had previously ranked first and second⁸⁸ in total acquisitions. If the three 1969 acquisitions survive the Department of Justice's suits, ITT will probably rank about seventh among U.S. industrials.⁸⁹

III. The Causes and Results of Mergers

Any firm, upon deciding to expand its operations, must choose between two paths to that goal: it may expand internally by enlarging its present plant or by constructing a new one, or it may acquire another firm that is already active in the particular field. Economist Samuel Reid points out that mergers claim a large share of the total funds spent in expansion. "Merger expenditures by manufacturing firms during 1967 amounted to about twelve billion dollars . . . over forty-three billion dollars of merger activity was recorded during 1968."⁹⁰

In this era of the free-wheeling conglomerate, it has been said that a merger's

potential rewards to management are great, and it is fairly predictable that those who do not rise to the challenge will be shouldered aside by the enterprisers who will. Indeed, large corporations are driven into "defensive" mergers to avoid take-over by others.⁹¹

It is, therefore, necessary to examine why there seems to be a need for bigness and why the merger has become such a popular method of attaining it.

A. Efficiency

In the early days of the new conglomerates, acquisitions were often made in the company's general area of expertise where it would "have at least some degree of familiarity, and where economies and efficiencies from assimilation are at least possible."⁹² In the last ten years, however, the large conglomerates have increasingly delved into new and unfamiliar areas in making their acquisitions. Examining this type of merger, economist John Blair says that "[o]f all types of merger activity conglomerate acquisitions have the least claim to promoting efficiency in the economic sense."⁹³ Unlike horizontal acquisitions, they provide no opportunity for pooling skills or knowledge gained in other operations and

86 *Id.* at 527.

87 *Id.* at 523.

88 *Id.* at 260.

89 *Id.* at 527.

90 Reid, *Mergers and the Economist*, 14 ANTITRUST BULL. 371 (1969).

91 Plaintiff's Answer to Comments of Defendant Northwest Indus., Inc., on Plaintiff's Response to Pretrial Order No. 1, at 17, *United States v. Northwest Indus., Inc.*, Civil No. 69C-1102 (N.D. Ill., filed May 21, 1969); *prelim. inj. denied*, 1969 Trade Cas. ¶ 72,853.

92 Turner, *supra* note 29, at 1315.

93 Blair, *The Conglomerate Merger in Economics and Law*, 46 GEO. L.J. 672, 679 (1958).

do not allow consolidation of operations by the closing down of less efficient plants. Unlike vertical acquisitions, they do not help to provide an orderly arrangement of the successive stages of the production-distribution process.

Geneen, however, argues that even in unrelated fields, "we can improve their efficiencies to make our valuation worthwhile to both sets of shareholders."⁹⁴ This will happen, he says, because mergers will result in economies in nearly every area of operation — management, distribution, production, and research. Each of these operations will have an optimum point at which it operates most efficiently; usually, the various optima will not converge at a single point. If things can be marketed faster than they can be produced, the excess capacity must be channeled elsewhere. In order to realize the potential saving represented by the excess capacity, a firm will continue to diversify until it can bring its various optima into equilibrium. It has been said that this "never-ending quest to utilize excess capacity and achieve economies may in itself induce growth."⁹⁵ Any unused equipment or ability offers an opportunity for saving, which, if used, would be a true economy of scale, i.e., one to the public economy as well as to the private firm.

It has also been urged that a larger firm can achieve economies of scale in regard to financing because of increased access to the money market. While it is true that "[o]ften the very fact that the large firm is diversified, or is diversifying, will contribute heavily to reducing the risk,"⁹⁶ it is questionable whether the risk is the main reason for the preferential loan, especially during times of tight money. Here, there is no excess capacity in the parent company that could be utilized. To the extent that capital is extended merely to gain favor with the parent company, no real saving exists in the public economy, although it may operate as a private benefit to the subsidiary and parent companies.

A similar situation arises in advertising or promotional expense. Here again, "[t]o the extent that quantity discounts reflect cost savings to the advertising media, the large firm's advantage is a true economy of scale, and is both a private and a social economy because it reduces the resources necessary to obtain any given promotional result."⁹⁷ As with capital costs, however, it is questionable how much represents merely a bulk discount to a large customer. Advertising discounts are more of a threat to a potential entrant than differences in capital costs, assuming a differentiable product. Disadvantage in the capital market is rarely substantial enough to prevent entry;⁹⁸ a firm with a product that can be differentiated, however, given sufficient conglomerate market power, will "tend to heighten the preferences of buyers for the product of the acquired firm, as well as to create for the acquired firm a more dominant position in its channels of distribution."⁹⁹ When this barrier to entry is present, a particular firm, when backed by the market power of a conglomerate, may help to reduce the barriers

94 Geneen, *supra* note 28, at 563.

95 J. NARVER, CONGLOMERATE MERGERS AND MARKET COMPETITION 64 (1967).

96 Turner, *supra* note 29, at 1338.

97 *Id.* at 1332.

98 *Id.* at 1338.

99 J. NARVER, *supra* note 95, at 128. Narver defines conglomerate market power as "the ability of a conglomerate firm at its discretion to shift marketing emphasis and resources among its markets and activities." *Id.* at 105.

enough to allow for its own entry; but this will, at most, cause a switch and not a breakdown of the barriers.¹⁰⁰ Narver argues that if the acquired firm "is relatively large in a market with an already moderate-to-high level of product-differentiation barriers, it is probable that the merger will increase these barriers and, therefore, will tend to lessen competition."¹⁰¹ The barriers are increased because "[p]romotional economies seem likely, as has been noted, to lead to more intensive, even if less expensive, promotional efforts than before," thus raising "the total 'starting-up' investment in promotional expense that a new-comer must make in order to break down entrenched consumer preferences for existing brands."¹⁰²

Advertising economies of scale, then, are normally private economies and, if anything, often have a harmful effect on the economy and on competition. Economies in capital, while also representing chiefly a private saving, can be considered more neutral, as their harmful effects are less serious. It is only in operational areas that economies that are at once public and private can occur. To the extent that these economies do occur, they foster economic growth and should be encouraged.

It is, however, questionable whether these economies will be more likely once the conglomerate has taken over operation of the small business. The Federal Trade Commission argues that

considerable uncertainty remains over the nature of efficiency gains to be derived from conglomeration. Analysts generally agree that common ownership is unlikely to yield significant production or marketing economies when the production processes used and the markets served are diverse.¹⁰³

Litton Industries has suggested that there are savings due to improvement in management technique; "the traditional concepts of management" exemplified by "the top-heavy bureaucratic institutions of early corporate firms" are being rejected.¹⁰⁴ But as the stars of the glamorous conglomerates of the recent past, like Martin-Marietta, "Automatic" Sprinkler Corp., and General Dynamics, become slightly tarnished, problems of managerial control and communications are usually cited as causes.¹⁰⁵ *Fortune* described the management of the merged Olin-Mathieson as a "loose confederation of tribal chieftains."¹⁰⁶ A verdict is not yet possible as to the long-range success of the new managerial techniques, but as Willard F. Rockwell warns:

Sooner or later, after all the crazy speculation, after all the manipulations, those acquisitions must be operated profitably. And it isn't easy to find the management. Conglomerates must cope with the problems of maturity — the inevitable day when the pace of expansion slackens. Then, without the continuous growth-through-merger that has too often been the base of their Wall Street appeal, the conglomerates will become indistinguishable

100 *Id.* at 134.

101 *Id.* at 129.

102 Turner, *supra* note 29, at 1336.

103 FTC REPORT 73.

104 *Id.* citing 1967 Litton Annual Report.

105 *Id.* at 75.

106 *Id.* at 116.

from such traditional multi-industry companies as General Electric. Only then will come the real test of whether they can survive and prosper. The conglomerates may indeed already be the corporate archetype of the future. They have yet to prove it.¹⁰⁷

Technological advantages may also turn into a mirage on closer inspection. Since a large firm has the most to gain from improvements in the production process or in the product itself, it is argued, it will have the incentive to develop the new methods; in markets of high concentration, where price competition is limited, improved products may be the only real method of increasing profits. The Cabinet Committee points out, however, that inventive zeal is often tempered by the realization that "the introduction of new concepts [and] modifications of the existing, expensive production facilities are costly and risky."¹⁰⁸

A survey of sixty-one various inventions found that less than half had been developed by inventors financed by or associated with business firms.¹⁰⁹ Of the twenty-five most important products and processes of Du Pont, fifteen were discovered outside its laboratories.¹¹⁰ These studies indicate that while large companies may spend large amounts in acquiring rights to new products or processes, they "allocate a significantly smaller proportion of total revenue to research than their smaller rivals, indicating, perhaps, that once a certain scale" is reached, there is no incentive to expand it.¹¹¹ It can also be argued that the percentage of income allocated declines because of increased efficiency; there is, however, strong enough evidence to cast doubt on the reliability of the very large firms as a source of technological innovation.¹¹²

The speed with which a new process (or a new product) will be incorporated into present production lines is dependent on three variables: (1) the degree of superiority that the new process offers, (2) the ease with which it can be merged into the present structure, and (3) the degree of risk that the introduction entails. Using these indicia, it is more probable that the relatively small firm, or even a new entrant, will first introduce a new process. This paradox is so because the initial investment required is smaller. It could also be argued, however, that the resulting savings would be greater and therefore more tempting to the larger firm. Closely allied to this is the risk, undoubtedly greater for the large company unless the process is introduced on a limited basis; in such a case, one of the arguments for the multiplant firm is destroyed. It is also argued, however, that the multiplant firm can test various processes in different plants and then select the superior process.

Nonetheless, the new firm remains the most likely to implement new processes, as it will suffer no loss on replaced machinery, will not have to worry about merging it into the present production line, and will probably be willing to take more of a risk to break into the business.

107 TIME, Mar. 7, 1969, at 80.

108 CABINET COMMITTEE STUDIES 64.

109 *Id.* at 66. The inventions included such varied and important items as the ball point pen, cellophane, television, xerography, the polaroid camera, and the automatic transmission.

110 *Id.*

111 *Id.* at 67.

112 See Knox, *Workable Competitive and Public Policy*, 1 ANTITRUST L. & ECON. REV., Spring, 1968, at 41, 69.

It is also questionable, as indicated above, whether the traditional theories of multiplant economies are still valid — if they ever were. As long ago as 1941, Dr. Frank Fetter questioned their validity:

It is apparent that the "economy of large production" in this sense is essentially a phenomenon of the single unit plant rather than of plural unit plants. It is a matter of internal arrangements and economies within a single plant. It is technical or technological, not financial or commercial; that is, it is the sum of various economies of time, materials, and wear and tear of machinery combined with labor used in a continuous process on one product as compared with a more or less discontinuous process with change of product and patterns. . . . It will be observed that combination by means of special holding companies or by ownership of stock in other corporations gives unity to the ownership, but not to the productive processes of the subsidiary companies. The physical plants and equipment remain largely under decentralized [*sic*] management; they still produce singly, while the officers of the controlling corporations are concerned almost wholly with financial and general organization and commercial matters. . . . Simple as is the distinction, when formally set forth, between a large single plant with its economy of mass production and a big business in the sense of the combined ownership of plural units, it is constantly ignored, either innocently or intentionally, with resulting great confusion of thought. . . . It is often implied and sometimes explicitly declared with an appearance of seriousness that any limitation of the size of corporations means a return to the hand tools and the small neighborhood shops of the Middle Ages. The exaggerations and error of such a statement surpass absurdity.¹¹³

Professor Bain's study showed that

[t]he economies of large multiplant firms are left in doubt by this investigation. In half the cases in which definite estimates were received, such economies were felt to be negligible or absent, whereas in most of the remainder of cases they seemed slight or small.¹¹⁴

The Cabinet Committee followed Bain, concluding that "in the vast majority of industries, plants capable of supplying no more than five percent of the national market are adequate to achieve all the advantages of large-scale production."¹¹⁵ In a few instances, the committee found multiplant savings of three to five percent of costs, but that even these could be achieved with two to four plants.¹¹⁶ Dr. John Blair, testifying before the Senate Subcommittee on Antitrust and Monopoly, reiterated his position that

the large plural-unit corporate enterprises are, if anything, less efficient than smaller concerns. At the very least, the widely held assumption that the ownership and control of plural production units by single corporate enterprises contributes to efficiency would seem to rest upon an overwhelming absence of supporting facts.¹¹⁷

¹¹³ *Hearings Before the Subcomm. on Antitrust and Monopoly of the Senate Comm. on the Judiciary*, 87th Cong., 1st Sess., 1776 (1965) [hereinafter cited as 1965 *Hearings*].

¹¹⁴ *Id.* at 1556.

¹¹⁵ CABINET COMMITTEE STUDIES 63.

¹¹⁶ *Id.* at 64.

¹¹⁷ 1965 *Hearings* 1556.

Even if a creative management is able to introduce innovations that will improve the acquired firm's performance, the result will not benefit the public economy because

a relatively large acquired firm in an already moderately-to-highly concentrated market, will in gaining a market share tend to increase concentration and thereby to decrease competition in the *long run*. Thus, while heightened competition among the large firms in a market is possible (not necessarily probable) because of the acquisition of a relatively large firm, such a merger, nevertheless, probably bodes ill for the total market competition in the long run.¹¹⁸

In producer-goods industries, where opportunities for technological innovation are greatest, market concentration has declined in the postwar years.¹¹⁹ On the other hand, concentration is increasing in consumer-goods industries where there is large-scale advertising to promote product differentiation.¹²⁰ The Cabinet Committee concluded that it is "the requirements and advantages of large-scale advertising, rather than technology" that has fostered the increase in concentration in the postwar period.¹²¹

B. The Deep Pocket

Wealth, of necessity, plays an important part in American business; without sufficient capital a business cannot survive. Accordingly, "the resources of the firm determine, in large part, what the firm perceives in the external world and how the firm responds to changes in that world."¹²²

Consequently as big business grows bigger and bigger, it becomes more and more necessary to look at exactly what result sheer financial might has on merger theory. In all mergers, even when the merging firms are more or less financial equals, "the financial effect is widely recognized and counted on in business affairs. Some economists deny its presence, but that denial usually is based on unrealistic assumptions about the degree of perfection in capital markets."¹²³ In the conglomerate firm, the wealth of the various divisions is even more important. This is so because "[i]n a particular market, events creating losses for one profit center may well have little or no effect on another. Conglomerates consequently have options for strategies in individual markets that are unavailable to other firms."¹²⁴ Funds to ease the pinch of declining sales and profits can then be shifted from another division. This is one reason why cyclical or high-risk firms prefer the security of conglomerate ownership.

Wealth can also be important in helping a smaller firm secure a more powerful position within the particular market or in helping a larger firm in-

118 J. NARVER, *supra* note 95, at 125-26.

119 CABINET COMMITTEE STUDIES 68.

120 *Id.* at 68-69.

121 *Id.* at 69.

122 J. NARVER, *supra* note 95, at 62.

123 Campbell & Shepherd, *Leading-Firm Conglomerate Mergers*, 13 ANTITRUST BULL. 1361, 1367 (1968).

124 FTC REPORT 398.

crease its dominance. In the ITT-Grinnell case¹²⁵ the government argued that

Grinnell is already the dominant firm in at least four lines of commerce, each of which is concentrated and for the most part comprised of relatively small firms with very little market power. ITT currently ranks as the eleventh largest industrial corporation in the United States and is growing rapidly. ITT will strengthen Grinnell's hold on these four lines of commerce by reciprocity effect, by placing all of the financial and economic resources a company of such magnitude can supply at Grinnell's disposal, and by adding to Grinnell's product mix many related product lines acquired by ITT in former acquisitions.¹²⁶

ITT, however, contended

that "ability to finance does not play a significant role in the sprinkler business * * *" . . . and that "Grinnell is already in a position to offer credit, finance and leasing opportunities to purchasers of sprinkler systems and needs nothing from ITT to do this as widely as it wishes."¹²⁷

On the other hand, in expressing opposition to the ITT-Hartford merger, the government argued that "Hartford's surplus of \$400 million" could be used "to finance the operation and expansion of ITT and its subsidiaries."¹²⁸ The government charged that "the addition of Hartford with its nearly \$2 billion in assets and \$400 million in excess of required surplus will mean a new source of financial backing and the ability to expand even faster."¹²⁹ This would be especially helpful to Levitt & Sons, the nation's largest residential home builder, which needs money to finance land purchases and construction as well as "a source of mortgage money for home purchasers."¹³⁰

ITT sneered at this argument, contending that if Hartford did not have the \$400 million surplus "the amount that ITT would be paying for Hartford would be decreased by the same figure."¹³¹ Since the additional funds could also be obtained through an offering of securities, "[a]ny 'access' that the present acquisition will give ITT to Hartford's 'surplus surplus' will thus be on terms that ITT could better by conventional financing procedures."¹³² Since the financing of a merger can be built into the transaction, however, the funds can be obtained at *no* cost to the acquiring firm.

Narver suggests that "[t]wo-way shifting is particularly probable when the

125 *United States v. International Tel. & Tel. Corp.*, Civil No. 13319 (D. Conn., filed Aug. 1, 1969), *prelim. inj. denied*, 1969 Trade Cas. ¶ 72,943.

126 Memorandum in Support of the Government's Motion for Preliminary Injunction, at 11-12, *United States v. International Tel. & Tel. Corp.*, Civil No. 13319 (D. Conn., filed Aug. 1, 1969), *prelim. inj. denied*, 1969 Trade Cas. ¶ 72,943.

127 Memorandum of International Tel. & Tel. in Opposition to Plaintiff's Motion for Preliminary Injunction, at 20, *United States v. International Tel. & Tel. Corp.*, Civil No. 13319 (D. Conn., filed Aug. 1, 1969), *prelim. inj. denied*, 1969 Trade Cas. ¶ 72,943.

128 Memorandum in Support of the Government's Motion for Preliminary Injunction, at 19, *United States v. International Tel. & Tel. Corp.*, Civil No. 13320 (D. Conn., filed Aug. 1, 1969), *prelim. inj. denied*, 1969 Trade Cas. ¶ 72,943.

129 *Id.* at 19-20.

130 *Id.* at 20.

131 Prehearing Memorandum of International Tel. & Tel. Corp. in Opposition to Plaintiff's Motion for Preliminary Injunction, at 43, *United States v. International Tel. & Tel. Corp.*, Civil No. 13320 (D. Conn., filed Aug. 1, 1969), *prelim. inj. denied*, 1969 Trade Cas. ¶ 72,943.

132 *Id.* at 44.

excess resources in the acquired firm are significant relative to the needs of the acquiring firm, or, generally, when the difference of size between the firms is not too great."¹³³ In the ITT-Hartford argument, an attempt is made to reduce this to deciding whether ITT is so huge and its resources so great that the addition of Hartford will not materially benefit its other divisions. Should this line of reasoning be accepted, it would be tantamount to saying that ITT is so powerful that it can do things that a smaller company would be precluded from doing merely because of its size. ITT's argument is therefore unsound; bigness does not confer such a special privilege or even operate as a mitigating factor in determining whether such a privilege should be granted.

Resources can be shifted

in either direction between the acquiring and acquired firms. The conglomerate is a global decision maker and two-way shifting is very likely. . . . The important point for the real-world analysis of conglomerate mergers is that resources *can* and *will* be shifted to whatever part of the conglomerate firm affords the greater long-run profit opportunities.¹³⁴

In discussing efficiencies, a distinction was made between public and private economies; in discussing the transfer of resources, it is necessary to distinguish within the private sector between that which is good for the conglomerate and that which is good for the individual firm. The two do not necessarily coincide. In opposing the Northwest Industries-Goodrich merger, the government pointed out that

[t]he large diversified firm, taking an over-all view of its interest, may adopt policies to promote its general welfare which would not be adopted if only the interests of the acquired firm were considered. See *U.S. v. Wilson Sporting Goods Co.*, 288 F. Supp. 543, 558 (N.D. Ill. 1968). The huge concern has its image to consider.¹³⁵

The problems arising because of the development of a network of interests among the leading firms will be discussed below in the section explaining the aggregate concentration theory.

Since "[m]anagement allocates resources among the activities of the firm in accordance with the primary goal of long-run profit maximization,"¹³⁶ it has been argued that a wealthy parent may subsidize a program of predatory pricing designed to drive the opposition out of business. The Federal Trade Commission expressed this fear in a 1947 report:

Threatened with competition in any one of its fields of enterprise, the conglomerate corporation may sell below cost or may use other unfair methods in that field, absorbing its losses through excessive profits made in its other lines of activity.¹³⁷

The predatory pricing may take one of three forms: (1) a multiproduct firm

133 J. NARVER, *supra* note 95, at 123.

134 *Id.* at 123-24.

135 Plaintiff's Answer, *supra* note 91, at 20-21.

136 J. NARVER, *supra* note 95, at 62.

137 *Id.* at 105.

may use product discrimination against single-product firms, (2) a multi-market firm may use geographic price discrimination against purely local firms, or (3) pricing according to product use may be employed against specialized competitors.¹³⁸

Turner, however, argues that "[t]he mere fact that a company can cover its losses with funds obtained elsewhere does not necessarily mean that it is going to be eager to do so."¹³⁹ He reaches this conclusion by balancing the losses incurred in the price war against the monopoly profits available after a victory, finding the profits insufficient. There will be no long-term profit, he argues, because if the monopoly profits are excessive enough to achieve a recoupment of losses, other firms will be drawn back into the market before the recoupment is completed or, at most, shortly afterwards. While theoretically appealing, this argument stumbles on practicality. Even ignoring traditional barriers to entry, the memory of a price war which decimated the then-existing competition and drove it out of the market will serve as a warning of what may happen to future entrants, thus precluding from the market all but the equally large firms.

There are, however, valid reasons for discounting this particular type of predatory pricing. In assuming that the practice will occur, one assumes that "the 'deep pocket' conglomerate will be bent upon a course of conduct which is not only illegal but criminal under other antitrust statutes, e.g., Section 3 of the Robinson-Patman Act, 15 U.S.C.A. Sec. 13a."¹⁴⁰ Since there are already severe penalties apart from divestiture proceedings, it is still possible to accept Turner's conclusion that "predatory pricing seems so improbable a consequence of conglomerate acquisitions that it deserves little weight in formulating antimerger rules based on prospective effects."¹⁴¹

Temporary price cuts designed to force a price policy on competitors, rather than to drive them out of business, is also a possible consequence of conglomerate market power. This type of policy is more likely, since the costs would be less, resulting in larger benefits. This practice, while harder to detect, is also illegal.¹⁴² Although some firms may not be detected in this maneuver, it is still too speculative a basis on which to build a conglomerate merger prohibition.

When dealing with wealth-theory situations, it is necessary to examine the market structure in order to determine what the results would be as

it is frequently only a relatively high magnitude of conglomerate market power that can affect market structure. . . . Thus, when both levels [concentration and barriers to entry] are high in a market characterized by differentiated oligopoly with at least some firms having conglomerate market power, a sizable "shock" must be injected into the market to alter its organization.¹⁴³

138 FTC REPORT 400.

139 Turner, *supra* note 29, at 1341.

140 Harsha, *The Conglomerate Merger and Reciprocity—Condemned by Conjecture?* 9 ANTITRUST BULL. 201, 221 (1964). The cited statute provides: "It shall be unlawful for any person . . . to sell, or contract to sell, goods at unreasonably low prices for the purpose of destroying competition or eliminating a competitor."

141 Turner, *supra* note 29, at 1346.

142 Robinson-Patman Act § 3, 15 U.S.C. § 13a (1964).

143 J. NARVER, *supra* note 95, at 136.

There is, however, a more subtle threat inherent in the market structure of industries in which conglomerates play leading roles. This was pointed out by Dr. Blair, who said that

[t]o most of the smaller producers these leading companies of American industry must loom as veritable giants. This is all the more true if the large company is primarily engaged elsewhere and its participation in the unconcentrated industry represents only a secondary activity. To any one of the hundreds of smaller firms in such industries the making of a competitive move which might involve retaliation by such a competitor could well appear to be an invitation to disaster.¹⁴⁴

There is no way short of structural relief to protect markets from this type of anticompetitive behavior.

C. Tax Advantages

In addition to radically restructuring the economy, the conglomerate merger, as McLaren sees it, is often based on financial considerations rather than on valid economic grounds.¹⁴⁵ This view is endorsed by SEC Chairman Hamer H. Budge, who believes that

more and more the basic reason for the merger or combination seems to be essentially a financial reason. That is, companies are buying other companies or merging with other companies because there are substantial immediate financial advantages to the surviving company in terms of increases in per-share earnings, and in terms of the liquid assets which can be obtained by acquiring other companies.¹⁴⁶

The Justice Department has argued that at the root of the "unprecedented flowering of conglomerate mergers" is "[t]he urge to amass greater power, to entrench managements by demonstrating a capacity to pyramid 'growth,' to make it possible to report higher per-share earnings, to do as well as the next fellow."¹⁴⁷ There are two interrelated financial considerations involved, each having its root in the accounting system used in effecting the merger.¹⁴⁸ The first consideration looks to Wall Street, where

merger battles often give a dizzy lift to stock prices long before actual mergers can create any fundamental economic values to underpin them. . . . This sort of thing perturbs some economists, who fear that the speculative fever could end in scandal or stock bust.¹⁴⁹

The second looks to Washington and the Internal Revenue Service for tax savings; although the immediate effect on tax revenue will be adverse, in the long run, the loss is often offset, because

144 1970 Hearings (testimony of Dr. John M. Blair).

145 TIME, May 23, 1969, at 100.

146 Hearings on Tax Reform Before the House Comm. on Ways and Means, 91st Cong., 1st Sess., 2367 (1970) (testimony of Hamer H. Budge).

147 Plaintiff's Answer, *supra* note 91.

148 See generally 1970 Hearings (testimony of Hamer H. Budge).

149 TIME, Feb. 21, 1969, at 78.

[t]o the extent that conglomerates increase taxable income by better management of acquired companies, or otherwise, they tend to generate additional government revenue. Thus, long-term revenue gains may well greatly exceed such short-term tax losses as may occur in connection with formation of conglomerate mergers.¹⁵⁰

In the mid-1950s, conglomerate acquisitions were normally financed through exchange of securities. The evolution of the price-earnings ratio as a prime determinant of value greatly promoted this type of acquisition. The price-earnings based system has developed from a stock investor's desire for "growth stocks," as opposed to high-return stocks. He sees the growth stock not only as a hedge against inflation, but also as an opportunity to come under the gentler capital gains tax. A further reason was suggested by SEC Chairman Budge:

Many investors do not have the knowledge or patience to interpret more complex financial statements and there is a tendency to look for simple rules of thumb — such as earnings per share, plus an indication that common stock of a particular company tends to sell at a particular multiple of earnings.¹⁵¹

The acquisition of low-multiple-earnings companies by high-multiple-earnings companies was thereby encouraged because it would result in a rising price-earnings ratio for the acquiring company.¹⁵²

According to Representative Mills, under this system, two companies with identical earnings and identical per-share earnings may sell at grossly different rates; a growth stock may be selling at thirty times earnings, while that of a more conservative low-debt company may be selling at fifteen times earnings.¹⁵³ In a takeover based on market value, there would be a two-for-one exchange. As a result, the surviving company's earnings would increase 100 percent with an accompanying increase in outstanding stock of only 50 percent. Consequently, "the surviving company's earnings would increase as a result of the merger, its reputation as a growth company would be enhanced and the price of its stock in relation to earnings would rise even higher."¹⁵⁴ The acquisitions director of one successful conglomerate said:

If the stock of your company is selling at twenty times earnings and you can find a company with steady earnings and competent management and stock selling at ten times earnings, buy it, regardless of what kind of business it is in.¹⁵⁵

Representative Wilbur Mills described the workings of the new system in this way:

If the company taken over was conservatively capitalized with a minimum of debt and distributed its earnings in the form of dividends, it paid taxes

150 W. MILLS, THE CONGLOMERATE MERGER TAX PROPOSAL, H.R. 7489, at 11 (1969).

151 *Hearings on Tax Reform*, *supra* note 146, at 15.

152 DeWind, *The Impact of Tax Factors*, 25 BUS. LAW. 765, 766 (1970).

153 W. MILLS, *supra* note 150, at 7.

154 *Id.* Mills says that results would be somewhat similar in a debt-equity exchange. *Id.*

155 Davidow, *Conglomerate Concentration and Section Seven: The Limitations of the Anti-Merger Act*, 68 COLUM. L. REV. 1231, 1238 (1968.)

on these earnings at the rate of approximately 50 percent. If it is taken over by means of debt securities, the shareholders are paid interest instead of dividends and the net income from the company taken over is increased by the tax benefit from paying interest, a deductible business expense, which amounts to about 50 percent of the interest. There may be an added financial advantage to the acquiring company: it may be able to use the taken-over company's assets to pay off that company's shareholders.¹⁵⁶ (Footnotes omitted.)

Out of this last concept, "the potential for paying the debt for the acquired company out of its own assets," there "arose the phenomenon of little companies staging forced take-overs of giants."¹⁵⁷

The equity security (stock) transaction, however, created problems of dilution, with each acquisition creating less of a favorable impact on the price-earnings ratio than the previous one. To avoid this problem, the new conglomerateers developed a method of exchanging long-term convertible debt, or debt with warrants, for the stock of the acquired company. The acquirer could pay out more in debt securities than the stock was selling for and could give interest payments that topped the dividend rate; at the same time, the acquiring company could step-up the basis of the acquired assets (it was a taxable transaction) and could pay tax-deductible interest payments instead of nondeductible dividends.¹⁵⁸ The earnings of the new company could more than pay the interest costs, with the result that the acquired company would finance its own acquisition. It is evident, then, that "[t]he interest deduction is the key to the whole transaction. Without that, the leverage of the situation is lacking."¹⁵⁹ Earnings are not diluted by additional stock, so the price-earnings growth would continue; this is because "[p]rofits of both firms are included, but they are divided only by the conglomerate's outstanding shares — a figure not changed by the merger."¹⁶⁰

In addition to the distortion of the price-earnings ratio, a wise choice of accounting methods will also allow a company to exaggerate its earnings for years following the merger. Usually, the "pooling of interests" method was the kindest to the conglomerate; one accounting professor compared the technique to a bikini: What they reveal is interesting, but what they conceal is vital.¹⁶¹

156 W. MILLS, *supra* note 150, at 6.

157 DeWind, *supra* note 152, at 767.

158 *Id.* This type of tax-deductible interest payment, while not prohibited outright, has been substantially curtailed by § 411 of the Tax Reform Act of 1969, INT. REV. CODE of 1954, § 279. The Act affects only those obligations issued after October 9, 1969, but assures even those covered by the Act of a minimum exemption of up to \$5 million of interest. In order for interest in excess of \$5 million to be disallowed, all of the following tests must be met:

(1) The obligation issued provides the consideration for an acquisition of stock or assets of another corporation, provided two-thirds of the total value of the assets were acquired in conjunction with an acquisition plan. Stock acquisitions remain exempt until the acquirer controls at least five percent of the voting rights;

(2) The obligation is subordinated to certain existing claims against the issuer;

(3) Certain convertibility (into stock) procedures are available; and

(4) The debt-equity ratio of the issuer exceeds two to one on the last day of a taxable year in which an acquisition described in (1) occurs or the issuer's projected earnings do not exceed three times the annual interest expense to be paid on the total indebtedness.

159 *Id.* at 768. See also *Hearings on Tax Reform*, *supra* note 146, at 15.

160 U.S. NEWS & WORLD REP., Mar. 24, 1969, at 87.

161 TIME, Mar. 9, 1970, at 62.

Under the pooling system "assets and liabilities of the two companies are simply added together at the time of merger and shown in the surviving company's balance sheet as if the two companies had always been one."¹⁶² An example will demonstrate the importance of this maneuver. Conglomerate A acquires Company B, which has assets with a depreciated or book value of \$2 million. In making the acquisition, Conglomerate A issues \$3 million in stock or debt securities. Under the pooling concept, these assets, which cost \$3 million, will be entered on the books at the \$2 million figure used by Company B. The extra \$1 million, although actually paid out to acquire the earning potential of Company B, will never be depreciated, amortized, or deducted from income in any way.¹⁶³ Earnings are thus overstated for years to come.

Under a "purchase" method of accounting, the acquiring company will assign an actual current market value, i.e., an apportioned amount of the total sum actually paid, and will depreciate it starting from this actual cost base. Since the purchase price for a going concern will often be greater than the total value of its aggregate assets, the difference between the current market value and the amount paid will be entered on the books as goodwill and amortized over a forty-year period. Under such a system, the expenditure is matched as closely as possible with the income that it generates.

While the purchase method appears to be the more sound of the two, it is not unanimously hailed, by any means. Of the practice of assigning new current values to acquired assets, one investment banker said: "They must be smoking opium."¹⁶⁴ Leonard Spacek, Chairman of Arthur Anderson & Co., says: "As far as I'm concerned, the Accounting Principles Board has gone off its rocker."¹⁶⁵ Although the Accounting Principles Board has drawn up an exposure draft dealing with this subject, its future is unclear. Since the SEC follows the regulations of the Accounting Principles Board, the decision will be closely studied. The great importance is shown by the increase in mergers during the last quarter of 1969 — a phenomenon that W. T. Grimm Co. attributes to the fear that the proposal will be adopted.

There may also be important tax considerations for the individual investor who is holding the debt securities of the acquiring company. Although in a merger effected through an exchange of common stock the investor could always claim a tax-free exchange, the shareholder under the new debt security system will be in an even better position because he may still "extend his tax liability over the 'life of the debt' or otherwise defer the liability to some extent." Often the debentures are convertible to stock; if the option is taken, the tax payment is further deferred until the stock is sold.¹⁶⁷ The system is not unanimously lauded, however. It has been argued:

The convertible debentures and stock warrants used by the acquiring con-

162 W. MILLS, *supra* note 150, at 8.

163 To see how this affected reported earnings of LTV and Gulf & Western, see Briloff, *supra* note 64, at 610. To see its effect on Xerox's acquisition of Scientific Data Systems, Inc., see Wall Street Journal, Feb. 27, 1970, at 1, col. 6.

164 Wall Street Journal, Feb. 27, 1970, at 16, col. 6.

165 *Id.* at 1, col. 6.

166 W. MILLS, *supra* note 150, at 7.

167 U.S. NEWS & WORLD REP., Feb. 24, 1969, at 86.

glomerate company to purchase the target company's stock from its shareholders are of "dubious long-term value" and may well be "worth far less than their immediate value or what they can currently be sold for."¹⁶⁸

This has been shown by the recent dip in fortunes of some of the "glamor" conglomerates.

As supply of attractive merging partners diminishes, the conglomerateer must continue to come up with newer and better methods and gimmicks to snare the prize. As a result of the shortage,

the prices paid for companies taken over in merger deals are getting higher. Cost of the acquired firm is now, on the average, about 21 times the firm's annual earnings, and about 21 percent more than the market value of the firm's stock.¹⁶⁹

This, when combined with the change in accounting rules, may be enough to put a substantial crimp in the merger movement.

D. Other Reasons for Mergers

In addition to those mentioned earlier, there are several other reasons why a firm should be allowed to become involved in a conglomerate merger, either as an acquiring or as an acquired firm.

As technology change proceeds at a faster and faster pace, the merger increasingly becomes the most attractive method of entering a new market, because "new facilities may be brought under operational control more quickly through mergers than internally."¹⁷⁰ In many industries, changes in marketing situations "are marked in months whereas once they were marked in decades";¹⁷¹ time is of the essence. Should a firm choose to start from scratch, it could conceivably find, upon opening its new plant, that the anticipated market has disappeared. On the other hand, should the firm choose to expand through merger, operations begin upon completion of the merger agreement.

Such an expansion is not only faster, it also presents a better picture in the financial statements as, in a merger, equipment is often purchased with little, if any, cash outlay. If the firm is well managed, the management can usually be retained; production personnel are trained and ready to work. Besides requiring a smaller cash outlay, the financing of a modern merger is usually built into the transaction. Perhaps most important, the going concern that is purchased has already demonstrated its earning power and the acceptability of its product.

The merger market may also increase competition by providing a market for owners who want to liquidate their businesses; knowing that a good firm is always marketable, small entrepreneurs will be more willing to plunge into business on their own. It is important to note, however, that the type of business that this is likely to encourage will not be of the calibre of that swallowed up, and often will not present effective competition for years to come; they will not be ready to

168 W. MILLS, *supra* note 150, at 12.

169 U.S. NEWS & WORLD REP., July 29, 1968, at 62.

170 J. NARVER, *supra* note 95, at 70.

171 FORBES, April 15, 1969, at 45.

immediately offer competition to an LTV or an ITT. Nonetheless, should the market be closed, it cannot be denied that this might "have adverse long-run effects on entry and growth of small business," as well as being "clearly against the interests of small businesses already in being."¹⁷²

Often an acquired company will have a business worth several million dollars, but the stock will be closely held or not easily marketable for some other reason. An equity security merger transaction with a conglomerate will give the owners

a substantial premium for their stock in a tax-free transaction. They receive a far more liquid asset . . . and any gain they realize is taxable only at capital gains rates. Usually, if the conglomerate operates like a holding company, the original management of the acquired company is retained and is allowed substantial autonomy.¹⁷³

Since the stock will probably increase in value, the owner has retained control over his company while liquidating his holdings on very favorable terms.

The merger also offers the stockholders of a larger firm a chance to use "corporate democracy," due to the increasing raids. A raid, like that on Goodrich, is usually made through a direct offer to the stockholders of the target company. Once the offer has been made, "[t]he stockholders are directly able to influence the direction of company policy and the composition of company management through acceptance or rejection of the offer for their stock."¹⁷⁴ In the case of a management antagonistic to the merger, the small stockholders may be listened to more closely in an attempt to get them to reject the tender offer.

The threat of conglomerate takeover may also be an incentive to sluggish firms, and even more so to sluggish industries, to get their companies moving again. Since it is this type of firm that makes a good target, "[m]any conglomerate mergers are . . . nothing more than takeovers of slothful firms, which need taking over or some other jolt. Indeed, much of the disapproval of conglomerates in the financial press reflects the natural resentment of settled financial interests against newcomers."¹⁷⁵ This was also recognized by FTC Chairman Weinberger, who admitted that the FTC

must also determine whether competition may be stimulated when the companies acquired by conglomerates have been "sleeping giants" long accustomed to the "easy life" and contributing little to the vigor of competition. Our policy should not be one which insulates an inefficient management from a corporate takeover that would in fact have the effect of adding a spur to competition by introducing, for example, new technology or price competition.¹⁷⁶

In this he agrees with Turner, who sees takeovers as "policemen" against shoddy management.¹⁷⁷

172 Turner, *supra* note 29, at 1326.

173 Davidow, *supra* note 155, at 1239.

174 W. MILLS, *supra* note 150, at 10.

175 Campbell & Shepherd, *supra* note 123, at 1361.

176 1970 Hearings (testimony of Caspar W. Weinberger).

177 *Id.* (testimony of Donald F. Turner).

C. William Verity, President of Armco Steel, the nation's fifth-largest steel-maker, agreed and said:

Jim Ling's taking over Jones & Laughlin was the best thing that ever happened to the steel industry. . . . Ling's move convinced them they had to diversify into businesses that earned a higher percentage of profits . . . or . . . end up as divisions in somebody else's company.¹⁷⁸

While beneficial in that it shakes up slow-moving companies, such take-overs, if Verity is right, will only hasten the merger movement and lead to a still greater degree of aggregate concentration. The remedy is, at best, a temporary antidote for sluggishness that could grow to be worse than the original disease. Once the revitalizing mergers have swallowed up the intermediate-sized companies, and when time has changed the innovators of today into the establishment of tomorrow (an establishment interlinked by a network of interests in various markets), who then will play the role of the catalyst? Furthermore, the defensive merger seldom makes good economic sense, as it is often a hastily contrived union created to avoid the "shotgun suitor." It will not necessarily insure better management. Dr. Briloff believes that, on the contrary, it may push the company to "uneconomic alternatives, take their liquid resources and use them for some kind of an acquisition, it matters not what for. Why? Because taken away the liquidity and the conglomerate is not looking at them . . . as a target."¹⁷⁹

The fear itself can be helpful, as it may transform "inefficient and ineffective management into more energetic and dynamic entrepreneurs."¹⁸⁰ This is especially true where there is a "hierarchy of the sons of forebears who succeeded to the presidency when they weren't at all that competent and in turn ran the mills into the ground,"¹⁸¹ as it will encourage a revitalized, if not a new management. Similarly, Goodrich would not have been ripe for a raid had the management run the company as daringly as they fought the merger. The resultant economic effect will depend on the type of defensive tactic adopted.

As big labor grows even more powerful, it is increasingly hard for the small businessman to deal effectively with it. Under the umbrella of the conglomerate, the balance is heavily weighted for the company because of the great amount of wealth and power aligned behind it; this is a corollary of the deep-pocket theory. As could be expected, organized labor is uncomfortable with the present trend.

It has also been said that "[c]onglomerate mergers do not remove a substantial competitor 'as an independent decision making force in the market' as is the case in horizontal mergers. They merely substitute 'one firm for another, leaving industry concentration as it was.'"¹⁸² While it is true that industry concentration does remain the same, there is an increase in aggregate concentration of power in a few hands. Although the firm may appear to remain as an independent decision-making force in the economy, ultimate decisions will now be made by the smaller number of businessmen who control the parent corporations.

178 BUS. WEEK, Oct. 11, 1969, at 168.

179 1970 *Hearings* (testimony of A. Briloff).

180 W. MILLS, *supra* note 150, at 11.

181 Geneen, *supra* note 28, at 568.

182 W. MILLS, *supra* note 150, at 10.

This was recognized by the court in *Wilson Sporting Goods*,¹⁸³ where it was pointed out that

[a] small group of large diversified firms competing against one another over a large range of products including those in the gymnastic apparatus field, would tend to reach somewhat different competitive decisions than those which small firms would reach, particularly where the threat of new entry had been considerably diminished.¹⁸⁴

Although not as great as is commonly thought, there are definite advantages to the conglomerate merger for the public, as well as the private interest. Whether they are sufficient to outweigh the dangers posed remains to be seen.

IV: The Aggregate Concentration Theory

A. The Offense Charged

In filing suit against Northwest Industries, the Justice Department contended that section seven had been violated, as competition would be decreased because

(d) The current trend of mergers of large firms will be furthered and encouraged, thereby (i) increasing the concentration of control of manufacturing assets, (ii) reducing the number of firms capable of entering concentrated markets, (iii) reducing the number of firms with the capability and incentive for competitive innovation, (iv) increasing the barriers to entry in concentrated markets, and (v) diminishing the vigor of competition by increasing actual and potential customer-supplier relationships among leading firms in concentrated markets.¹⁸⁵

Although other grounds were alleged that would possibly have been sufficient in themselves, this was the basis for the suit.

In filing suit, the Department of Justice was acting in accordance with the report of the Cabinet Committee, which urged the agencies to "step up merger enforcement efforts to prevent conglomerate-type mergers that weaken competition by removing significant potential competitors, raising entry barriers, and increasing business reciprocity opportunities."¹⁸⁶

Donald Turner had rejected this type of suit because he did "not believe Congress has given the courts and the FTC a mandate against 'superconcentration' in the absence of any evidence of harm to competition."¹⁸⁷ The government was now able to change the policy set by Turner, because it now believed that the superconcentration itself would be sufficient harm. Both sides could point to authorities to support their view. Adelman had said that "a truly conglomerate merger cannot be attacked in order to maintain competition, because it has no

183 *United States v. Wilson Sporting Goods Co.*, 288 F. Supp. 543 (N.D. Ill. 1968).

184 *Id.* at 558.

185 Complaint at 18, *United States v. Northwest Indus., Inc.*, Civil No. 69C-1102 (N.D. Ill., filed May 21, 1969), *prelim. inj. denied*, 1969 Trade Cas. ¶ 72,853.

186 CABINET COMMITTEE STUDIES 84.

187 Turner, *supra* note 29, at 1395.

effect on any market structure.”¹⁸⁸ Narver, on the other hand, said that “our analysis suggests that even the ‘truly conglomerate’ (pure investment) merger can have an effect on market structure and hence on competition.”¹⁸⁹ In order to determine which party is correct, it is necessary to examine the allegations set out in the complaint.

As was shown at the beginning of this paper, there has been a significant increase in concentration of control of manufacturing assets, which was the first objection cited in the complaint. The Cabinet Committee pointed out that “[t]he deconcentration which occurred in many industries since World War II would not have occurred had leading firms been permitted to make significant horizontal mergers.”¹⁹⁰ This argument can be transferred to the conglomerate merger area because of the snowball effect of a merger. This was shown when Wilson Sporting Goods tried to take over Nissen Corporation, one of several small companies involved in the gymnastic apparatus field. In refusing to allow the merger, the court said that

[p]reviously, the other firms in the industry were doing well enough on their own so that they did not want to sell out, or did not think themselves large enough to do so. . . . But since the news of the proposed merger, several of the small companies have become seriously worried about their ultimate survival and are considering the possibility of merger with larger firms.¹⁹¹

In this way, a merger can spark a chain of defensive mergers that will rapidly transform the face of the industry. The government, in the ITT-Hartford case,¹⁹² pointed out that “[a]cquisitions involving insurance companies have played an increasingly important part in the merger movement; in 1968 alone, there were over 200 mergers involving insurance companies.”¹⁹³

A similar argument was made in ITT-Grinnell,¹⁹⁴ where the government contended that “Grinnell’s small competitors are apt to suffer additional competitive disadvantages, other mergers by these companies will be triggered and the trend of acquisitions of leading firms in concentrated markets by large companies will be augmented.”¹⁹⁵

Since “[t]he Supreme Court has repeatedly emphasized that it is an important goal of Section 7 of the Clayton Act to preserve the long-run possibility of eventual deconcentration of highly concentrated industries,”¹⁹⁶ it hardly seems in keeping with the spirit of the Court’s decision to allow concentration via a merger wave to invade industries that are now deconcentrated. Through such a series

188 J. NARVER, *supra* note 95, at 118.

189 *Id.* at 119.

190 CABINET COMMITTEE STUDIES 84.

191 *United States v. Wilson Sporting Goods Co.*, 288 F. Supp. 543, 558 (N.D. Ill. 1968).

192 *United States v. International Tel. & Tel. Corp.*, Civil No. 13320 (D. Conn., filed Aug. 1, 1969), *prelim. inj. denied*, 1969 Trade Cas. ¶ 72,943.

193 Complaint at 7, *United States v. International Tel. & Tel. Corp.*, Civil No. 13320 (D. Conn., filed Aug. 1, 1969), *prelim. inj. denied*, 1969 Trade Cas. ¶ 72,943.

194 Complaint at 7, *United States v. International Tel. & Tel. Corp.*, Civil No. 13319 (D. Conn., filed Aug. 1, 1969), *prelim. inj. denied*, 1969 Trade Cas. ¶ 72,943.

195 Memorandum in Support of the Government’s Motion for Prelim. Inj. at 3, *United States v. International Tel. & Tel. Corp.*, Civil No. 13319 (D. Conn., filed Aug. 1, 1969), *prelim. inj. denied*, 1969 Trade Cas. ¶ 72,943.

196 Campbell & Shepherd, *supra* note 123, at 1378.

of mergers, an industry characterized by small independent companies and healthy competition can be changed into one controlled by a group of conglomerates or large businesses already linked by a community of interests.

If the link is not yet forged, Attorney General Mitchell argues, "the 200 largest manufacturing corporations are diversifying so quickly that at the present rate, a significant number will soon be facing each other in several markets."¹⁹⁷ There is thereby created "a 'community of interest' which discourages competition among large firms and establishes a tone in the marketplace for more and more mergers."¹⁹⁸ Mitchell points out that this community of interest need not be "a formal agreement but merely the recognition of common goals by large diversified corporations. . . . It posits that large diversified corporations may have little interest in competing with each other in concentrated markets."¹⁹⁹ As was shown earlier, the top 100 firms are rapidly entrenching themselves as leaders in several industries. Consequently, the large conglomerate may shrink from active competition in one market because of fear that, through retaliatory moves, the competition would spread to other markets, resulting in a multi-industry battle. Turner, however, fails to see a probability of programs of conglomerate forbearance. He says that

[i]f a conglomerate company is vulnerable to retaliation in markets other than that in which it attempts to assert a competitive advantage, one immediately asks why its vulnerability has not previously been exploited. Why has its competitor desisted up to this point? One could say that the competitor has desisted because it fears retaliation in a market in which it is vulnerable; but that merely takes us around in a circle, leaving much the the same question unanswered.²⁰⁰

Turner's argument neglects the basic drive of self-preservation. There are few individuals and few companies who will risk destroying or injuring themselves in an attempt to injure another. Accordingly, firm A, which has relatively weak subsidiaries in industries X and Y, will hesitate to compete vigorously against firms B and C in industry Z, where A is dominant, because B and C could then apply pressure in industries X and Y, where they are dominant.

The same practice may develop without the aforementioned fear of retaliation. Over the years, it has been found that "when corporations become large and conglomerated, they tend to accord special treatment to other large national and even international corporations."²⁰¹ There is not necessarily an agreement, but merely a realization that big companies should stick together, thus creating a "clubbish" atmosphere. As early as the 1920s, Irene du Pont tried to establish an esprit de corps among the country's "great corporations."²⁰²

Also, as was pointed out earlier, "[t]he huge concern has its 'image' to consider."²⁰³ A firm that follows certain pricing, marketing or other competitive

197 *Address of John N. Mitchell, supra* note 2, at 96.

198 *Id.* at 93.

199 *Id.* at 95.

200 1970 *Hearings* (testimony of Donald F. Turner).

201 FTC REPORT 461.

202 *Id.* at 462.

203 Plaintiff's Answer, *supra* note 91, at 20-21.

policies in one industry will usually adopt the same techniques in another. Du Pont, for example, would hardly do anything to jeopardize its standing (among other businesses) as a "great corporation."

The relaxation of competition would occur not only in pricing, thus preventing multi-industry price competition, but could easily spread into nonprice areas, as was charged in the the third section of the Northwest Industries complaint, with the result that competitive innovation is stifled. The fear of retaliation in other fields will prevent one company from disrupting the gentleman's agreement-like community of interests. In this way, one firm will not be able to achieve monopoly or near-monopoly in one industry, but a number of giant firms will eventually achieve a joint monopoly over American business.²⁰⁴

It is also charged that because of the present merger trend, there is a decreasing number of firms capable of entering concentrated markets. Destruction of potential competition is a recognized threat to competition and has been condemned by the Supreme Court.²⁰⁵ The significance of potential competition is usually determined by looking at such interrelated concepts as the structure and competitiveness of the relevant market, the likelihood of entry, and the number of potential entrants.²⁰⁶

Structurally, the number of sellers must be small enough that the price can be maintained above the normal competitive level. Turner argues that the number of potential entrants is not important; the relevant factor is that the firm be recognized as the most likely, or one of the few likely entrants.²⁰⁷ Combining these two factors, he contends that as economies of scale rise, fewer potential competitors are needed.²⁰⁸ This is because with large economies of scale, the potential competitor, upon entering the market, is likely to operate on a level that would take advantage of these economies; as a result, a larger share of the market is threatened, so those already in the market will be less inclined to raise prices high enough to encourage potential competitors to enter. This argument, however, neglects basic probabilities and assumes that all potential competitors, given the same situation, will react in an identical manner. This is simply not the case; the decision-making process is not that mechanical. Each firm will compare present market conditions to its own resources, goals, etc. Different facts will have different effects on each company. While five potential entrants instead of one will not pose a threat five times as large, the situation will, nevertheless, be vastly changed; but thirty firms will not necessarily be more beneficial than twenty. Turner also holds that barriers to entry cannot be so high that a potential entrant would, in order to recoup his expenses, be required to charge a price above the optimum price of those already in the industry.

204 Dr. Blair agrees, saying that if the 200 largest corporations hold a substantial share of the industrial economy, it inevitably follows that they will be important factors in a number of "individual economic markets." And where this is true, there will be present certain specific dangers to competition which would otherwise not exist. 1970 *Hearings* (testimony of Dr. John M. Blair).

205 See *FTC v. Proctor & Gamble*, 386 U.S. 568 (1967); *United States v. Penn-Olin Co.*, 378 U.S. 158 (1964); *United States v. El Paso Natural Gas Co.*, 376 U.S. 651 (1964).

206 AMERICAN BAR ASSOCIATION, SECTION OF ANTITRUST LAW, ANTITRUST DEVELOPMENTS 1955-1968, at 85-86 (1968).

207 Turner, *supra* note 29, at 1363.

208 *Id.*

Even if his three conditions are met, Turner sees the effect as insubstantial because a company can continue to charge high prices until a potential entrant makes a move to come in. It can then immediately drop the price down to the normal level, and since the potential competitor has not yet made financial commitments, he will divert his investment to some other industry. Once a beginning is made, however, it is too late. The company will then not only have to drop its prices, but it will also probably lose a share of the market to the new entrant, with a resultant plunge in profits.

While companies will be encouraged to keep their costs down, so that they could rapidly lower their prices in the event of entry by a potential competitor, Turner sees only one instance where acquisition of a potential competitor will have an effect on competition: the acquisition of a "substantial seller in a tight oligopoly by the most likely, or by one of the two or three most likely potential entrants."²⁰⁹ In other cases, he believes that the existence of a significant adverse competitive effect is too speculative and remote to deserve treatment, in and of itself, as a decisive factor against a merger.²¹⁰

The courts, however, have taken a somewhat more critical view of the competitive effects of destruction of potential competition. In the first of the potential competition cases to reach the Supreme Court, *United States v. El Paso Natural Gas Co.*, El Paso and Pacific Northwest, the acquired company, did not sell in the same market. Pacific Northwest, however, before the takeover, had tried to move into the California area where El Paso operated. In forbidding the takeover the Court said: "We would have to wear blinders not to see that the mere effort of Pacific Northwest to get into the California market, though unsuccessful, had a powerful influence on El Paso's business attitudes within the state."²¹¹ At the time, Pacific Northwest was the only other major interstate pipeline in the western states.²¹²

Under the rule developed in the second case, *United States v. Penn-Olin Co.*,

it is not necessary to show that a potential entrant will actually enter or that it had attempted to do so in the past. Rather, in some market situations the existence of potential competition may be a significant competitive force in itself even though actual entry never occurs.²¹³

Unlike *El Paso*, here neither firm was active in the market; both of the joint venturers, however, were considering it. Even though a new unit was added to the market, the joint venture was restrained because one potential competitor nonetheless disappeared. The Court said that

[t]he existence of an aggressive, well equipped and well financed corporation engaged in the same or related lines of commerce waiting anxiously to enter an oligopolistic market would be a substantial incentive to competition which cannot be underestimated.²¹⁴

209 *Id.* at 1365.

210 *Id.*

211 376 U.S. at 659.

212 *Id.* at 658-59.

213 ABA, *supra* note 206, at 86.

214 378 U.S. at 174.

In a third case, *FTC v. Procter & Gamble*, little was added to the doctrine laid down previously. This case was the reverse of *El Paso*; here, the acquiring firm wished to use the acquisition as a means of entering a new market, household bleach. Although Procter & Gamble denied that it would have entered the bleach market otherwise, the Court found that it was the most likely entrant, that it was diversifying into similar areas, and that it had easy access to all the prerequisites for entry.²¹⁵ After examining the market structure, barriers to entry, the number of potential entrants, and the likelihood of Procter & Gamble's independent entry, the Court held that the merger could not be allowed.

Potential competition may also be affected by barriers to entry. In *Procter & Gamble*, the Court observed that

[t]he acquisition may also have the tendency of raising the barriers to new entry. The major competitive weapon in the successful marketing of bleach is advertising. . . . Procter would be able to use its volume discounts to advantage in advertising Clorox. Thus, a new entrant would be much more reluctant to face the giant Procter than it would have been to face the smaller Clorox.²¹⁶

Because of advertising similarities, the merger had

enabled Clorox to "save" \$138,500 on advertising for a twelve-month period. Thus any potential entrant into Clorox's market, unless the potential entrant is very large, must consider the significantly enlarged disadvantage of promotion economies.²¹⁷

Even had this been a true economy, and not merely a private saving, it would not have saved the merger; the Court said that "[p]ossible economies cannot be used as a defense to illegality."²¹⁸

Closely allied to the use of wealth or market power to practice predatory pricing, which was discussed above, is the practice of reciprocal trading; unlike predatory pricing, however, another firm is involved in reciprocity. In bringing a suit against ITT and Hartford, the Department of Justice defined reciprocity as "a seller's practice of utilizing the volume or potential volume of its purchases to induce others to buy its products or services."²¹⁹ Apart from this overt practice, the Department of Justice pointed out a more subtle tactic which it calls reciprocity effect. It defines this as "the tendency of a firm selling or desiring to sell to another to channel its purchases to that company."²²⁰ Of the two, reciprocity effect is more elusive because "by definition the effect exists without any overt effort on the part of the favored firm. In order to cure 'reciprocity effect,' structural relief is necessary."²²¹

Reciprocity can be further broken down into three types: (1) one firm

215 386 U.S. at 580.

216 *Id.* at 579.

217 J. NARVER, *supra* note 95, at 130.

218 386 U.S. at 580.

219 Complaint at 7, *United States v. International Tel. & Tel. Corp.* Civil No. 13320 (D. Conn. filed Aug. 1, 1969), *prelim. inj. denied*, 1969 Trade Cas. ¶ 72,943.

220 *Id.*

221 "Tenth and Constitution Ave. N.W.," Address by W. Comegys, New England Anti-trust Conference, Boston, Massachusetts, Oct. 3, 1969.

threatens to withdraw patronage unless the other makes reciprocal purchases, (2) two firms practice reciprocity by mutual agreement, and (3) one firm suggests to a supplier that reciprocal purchases would be appreciated.

Reciprocity enjoys near-universal condemnation because it "distorts the pattern of trade away from the ideal, with no compensating economic advantage."²²² There is no economic advantage because

[b]y unfairly diverting business from competitors of the participants, the practice works a departure from the process of open competition in which each industrial purchaser theoretically seeks out that supplier who will give him the best product at the lowest cost.²²³

There is no public economy involved, because "reciprocity does not contribute to the total magnitude of trade; it merely rechannels it."²²⁴

There is, however, another school of thought that considers reciprocity a "hobgoblin." As Professor Bork sees it, "[i]f a company is using its position as an important customer to bargain the best possible prices from its suppliers, then that company has no market power left to force the suppliers to buy from it on noncompetitive terms."²²⁵ As with many theories, this is appealing on the surface but simply does not measure up to reality. Reciprocity, although hard to detect, does play a significant role in corporate purchasing habits. In a 1961 poll of 300 purchasing agents made by *Purchasing Magazine*, it was shown that 51 percent considered reciprocity to be a significant factor in their purchasing habits; more importantly, 78 percent of those companies with sales of over \$50 million used reciprocity in making their purchases.²²⁶ Shifting of purchases is a painless way of keeping supplier-customers happy. By careful purchasing habits, a purchasing agent can assure a steady reciprocal purchase. Under this system, the seller will only have to *meet*, and not *better*, the offer of his competitor. The competitor, therefore, cannot win; if he drops his price, a corresponding cut by the reciprocal trader will retain the contract. The market is foreclosed; he cannot break in.

In 1965, the Supreme Court prohibited a merger because the acquiring firm used a reciprocity program.²²⁷ The Court recognized that "[r]eciprocal trading may ensue not from bludgeoning or coercion but from more subtle arrangements," and held that "[r]eciprocity in trading as a result of an acquisition violates §7, if the probability of a lessening of competition is shown."²²⁸

Since reciprocity "can be eliminated only by forestalling the creation of the conglomerate structure that fosters it,"²²⁹ once the Court found that reciprocity was practiced the merger was dissolved. In a concurring opinion, Mr. Justice

222 Turner, *supra* note 29, at 1387.

223 ABA, *supra* note 206, at 11.

224 FTC REPORT 328-29.

225 FORTUNE, Sept., 1969, at 160.

226 *Address of John N. Mitchell, supra* note 2, at 94.

227 FTC v. Consolidated Foods, 380 U.S. 592 (1965).

228 *Id.* at 594-95.

229 Turner, *supra* note 29, at 1390. This may be contrasted with Professor Turner's recent comments before a Senate subcommittee:

[T]he potentiality of reciprocity deserves to be all but disregarded in calculating the likely consequences of a conglomerate merger. . . . I would disregard it in the merger area not because invidious reciprocity can be largely eradicated by a direct approach under existing law 1970 Hearings (testimony of Donald F. Turner).

Stewart, recognizing that "large scale diversity of industrial interests almost always presents the possibility of some reciprocal relationships," said that "the opportunity for reciprocity is not alone enough to invalidate a merger under §7."²³⁰

Mr. Justice Stewart's opinion seemed to be in direct opposition to the Third Circuit, which had previously said that

the mere existence of this purchasing power might make its conscious employment toward this end unnecessary; the possession of the power is frequently sufficient, as sophisticated businessmen are quick to see the advantages in securing the good will of the possessor.²³¹

Consequently, in the ITT-Grinnell case,²³² the government argued that "[e]ven without any illegal activities on the part of the merging firms, a merger that merely creates a structure conducive to significant reciprocal dealing is illegal under Section 7."²³³ Since "opportunities for reciprocity increase geometrically as an enterprise becomes larger and more diversified,"²³⁴ this argument would hold nearly all conglomerate mergers illegal.

On the other hand, it has been suggested that

potential reciprocity will not be an argument likely to invalidate very many conglomerate mergers. . . . [I]f the required firm, has, say, less than 20% of its market, there is not sufficient concentration to call Section 7 into play. Secondly, if most conglomerate firms adopt resolutions forbidding reciprocity, the presumption that their protestations of innocence are truthful can only be overcome by detailed behavioral evidence.²³⁵

In 1969, however, in *Allis-Chalmers Manufacturing Co. v. White Consolidated Industries, Inc.*,²³⁶ the Third Circuit adhered to its decision in *Ingersoll-Rand*, saying:

An acquisition which creates a market structure conducive to reciprocal dealing presents the acquiring company with an advantage over competitors, an advantage which by its very nature is anticompetitive. . . . And the reciprocal trading made possible by such an acquisition need not ensue "from bludgeoning or coercion."²³⁷

As the case was still at the preliminary injunction stage, the court did not consider market share in making its decision, although it did indicate that since Allis was "one of a small number of sellers who account for a significant share of the market," it would be less concerned

with the asserted small percentage of total steel purchases, nationwide,

230 380 U.S. at 603.

231 *United States v. Ingersoll-Rand Co.*, 320 F.2d 509, 524 (1963).

232 *United States v. International Tel. & Tel. Corp.*, Civil No. 13319 (D. Conn., filed Aug. 1, 1969), *prelim. inj. denied*, 1969 Trade Cas. ¶ 72,943.

233 Memorandum in Support of the Government's Motion for Preliminary Injunction at 15, *United States v. International Tel. & Tel. Corp.*, Civil No. 13319 (D. Conn., filed Aug. 1, 1969), *prelim. inj. denied*, 1969 Trade Cas. ¶ 72,943.

234 *United States v. Northwest Indus., Inc.*, Civil No. 69C-1102 (N.D. Ill., filed May 21, 1969), *prelim. inj. denied*, 1969 Trade Cas. ¶ 72,853.

235 Davidow, *supra* note 155, at 1267; *see also* ABA, *supra* note 206, at 88-89.

236 414 F.2d 506 (3d Cir. 1969), *cert. denied*, 90 S. Ct. 567 (1970).

237 *Id.* at 518.

which a White-Allis combine would account for than with a comparison of the dollar volume of steel purchases by such a combine vis-a-vis the dollar volume of steel purchases by White's competitors.²³⁸

Recently, in the *Northwest Industries* case,²³⁹ the government urged the court to expand the concept of potential reciprocity still further. The government urged that

it is not mandatory that a proper product mix be established between Northwest-Goodrich and Company X, if Northwest-Goodrich can prevail on a supplier to "put out the red carpet" for Northwest-Goodrich. In view of the effect of the subtle leverage provided by reciprocity, there is compelling reason for assuming that the merger may adversely affect, through foreclosure resulting from reciprocity and/or reciprocity effect, every line of commerce in which either firm is engaged.²⁴⁰

Although it is undoubtedly true that the merger created a structure through which Northwest could enlist its suppliers in a reciprocity program, this alone would seem to be far too speculative a basis on which to forbid the merger.

The reciprocity partners may be linked by something other than reciprocal purchases. The Federal Trade Commission pointed out that "conglomerate forbearance between potential competitors can induce a potential entrant to use the possibility of entry as consideration in exchange for a reciprocal favor,"²⁴¹ Koppers Company, Inc., used this type of reciprocity in its dealings with Du Pont. The process was revealed in a memorandum in Du Pont's files:

Koppers Company is exploring the possibility of manufacturing their own oleum. We are currently the supplier and the volume amounts to close to \$500,000 per year. In view of the potential decision to build an oleum plant, they have become concerned about their business with Du Pont and asked for an opportunity to visit us to discuss their reasons for considering such a venture and to go over the potential sales possibilities with Du Pont.²⁴²

No matter what type of reciprocity is being considered, however, it is difficult to argue with the government when, in opposition to the Northwest Industries-Goodrich merger, it said that the proliferating large-firm mergers are "multiplying opportunities for reciprocity over the expanding range of markets in which an ever fewer number of highly diversified firms will find themselves competing."²⁴³

As the opportunities for reciprocity increase, so does the likelihood that it, or at least reciprocity effect (which exists without any overt effort), will have a still more serious effect on competition.

B. The Legislative History

In 1914, the distress over the merger movement culminated in the passage of

238 *Id.* at 521.

239 *United States v. Northwest Indus., Inc.*, Civil No. 69C-1102 (N.D. Ill., filed May 21, 1969), *prelim. inj. denied*, 1969 Trade Cas. ¶ 72,853.

240 Plaintiff's Answer, *supra* note 91, at 12-13.

241 FTC REPORT 463 (footnote omitted).

242 *Id.* at 464.

243 Plaintiff's Answer, *supra* note 91, at 19.

the Clayton Act.²⁴⁴ Section seven of the Act,²⁴⁵ which dealt with mergers, originally covered only acquisitions made by purchasing the stock of another company. Since this was the ordinary method of acquisition (purchase of assets was rare), "there was relatively little immediate need . . . for Section 7 to deal with asset acquisitions."²⁴⁶ As a result, the government was powerless when the companies shifted merger tactics and began to effect their mergers through an acquisition of assets. Between 1927 and 1949, twenty-one separate bills to amend section seven were introduced in Congress;²⁴⁷ in 1950, these efforts came to fruition with the passage of the Celler-Kefauver Act. Through this Act, section seven was amended to read:

That no corporation . . . shall acquire, directly or indirectly, 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 of such acquisition may be substantially to lessen competition, or tend to create a monopoly.

In 1962, the Supreme Court, in *Brown Shoe Co. v. United States*,²⁴⁸ took its first careful look at the amended statute. Because there was such extensive attention given by Congress to the wording of the statute, the Court decided that it would carefully review the legislative history as found in the hearings, committee reports, and floor debate in determining the meaning of the rather general language of the Act.²⁴⁹

In examining the legislative history, the Court found that

[t]he dominant theme pervading congressional consideration of the 1950 amendments was a fear of what was considered to be a rising tide of economic concentration in the American economy. . . . Other considerations . . . were the desirability of retaining "local control" over industry and the protection of the small businesses.²⁵⁰

It is apparent that Congress, in referring to concentration, meant aggregate concentration as well as market concentration.²⁵¹ At the hearings, Celler testified: "Great masses of economic power and monopoly stunt the growth of the individual enterprise and kills [sic] individual ambition and individual dignity."²⁵² The Senate report bluntly stated that the purpose of the bill was "to limit future increases in the level of economic concentration resulting from corporate mergers and acquisitions."²⁵³ Both the House and Senate reports refer to the startling increase in levels of *aggregate* concentration — the statistics do not refer to *markets* — as proof that the amendment was needed.²⁵⁴ The Senate report con-

244 Clayton Act, 15 U.S.C. § 12 (1964).

245 *Id.* § 7, 15 U.S.C. § 18 (1964).

246 J. NARVER, *supra* note 95, at 34.

247 *Id.* at 38.

248 370 U.S. 294 (1962).

249 *Id.* at 312, 315.

250 *Id.* at 315-16.

251 R. Donnem, *Antitrust and the Super-Conglomerates — a Look at the Law Books*, Address at the American Management Association Briefing Session, New York, New York, Nov. 10, 1969, in 5 CCH TRADE REG. REP. ¶ 50,263, at 55,574.

252 J. NARVER, *supra* note 95, at 44.

253 2 U.S. CODE CONG. & AD. NEWS 4295 (1950).

254 *Id.*

cludes its discussion of the level of concentration by saying that "[t]he enactment of the bill will limit further growth of monopoly and thereby aid in preserving small business as an important competitive factor in the American economy."²⁵⁵

In examining the effect of concentration on small businessmen, Dr. Blair testified at the hearings that

the conglomerate type of acquisition is one which is peculiarly dangerous to small business. A company that is so diversified is in a position to strike out with great force against any smaller company which may seek to compete with it in any one of the variety of fields in which it is engaged and, of course, it is able to make up whatever losses that are incurred in the competitive war with its profits secured in other fields in which it is engaged.²⁵⁶

Likewise, Professor Adams testified that "[c]onglomerate size is a problem in a competitive system The conglomerate firm, by virtue of its diversification, can discipline or destroy its more specialized competitors."²⁵⁷ In *Brown Shoe*, while examining the effect of concentration on the small businessman, the Court, in a footnote,²⁵⁸ cited the remarks of Senator Kefauver during debate:

The control of American business is steadily being transferred . . . from local communities to a few large cities in which central managers decide the policies and the fate of the far-flung enterprises they control. Millions of people depend helplessly on their judgment. Through monopolistic mergers the people are losing power to direct their own economic welfare. When they lose the power to direct their economic welfare they also lose the means to direct their political future.²⁵⁹

These effects were obviously antagonistic to the traditional goals of the anti-trust laws, which had sought "to perpetuate and preserve, for its own sake and in spite of possible cost, an organization of industry in small units which can effectively compete with each other."²⁶⁰

Also cited by the Court in *Brown* were the remarks of Representative Bryson, who said that "the existing concentration of economic power threatens our basic liberties and is detrimental to progress in this country."²⁶¹ At the hearings, this point had been raised by Representative Celler:

How far should government, the people, allow that kind of concentration, which for want of a better name we call conglomerate concentration to proceed? . . . You get to a point where it is so large that it affects the lives and happiness of so many people, that as a matter of fact, you could not let it fail.²⁶²

Congressman Patman echoed this concern, saying: "Merger must be stopped

255 *Id.*

256 J. NARVER, *supra* note 95, at 45.

257 *Id.*

258 370 U.S. 294, 316 n.28 (1962).

259 96 CONG. REC. 16452 (1949).

260 *United States v. Aluminum Co. of America*, 148 F.2d 416, 429 (2d Cir. 1945).

261 95 CONG. REC. 11494 (1949).

262 J. NARVER, *supra* note 95, at 47.

now, or else the big corporations will become so big that there will be nothing left to do except for the Government to take them over."²⁶³

While the amendment was not aimed solely, or even chiefly, at conglomerate mergers, it is clear that they are covered by the Act. Representative Boggs, in discussing the amendment, said:

A third avenue of expansion — and this is one of the most detrimental movements to a free enterprise economy — is the conglomerate acquisition. . . . [T]hey build up huge business enterprises which enable them to play one type of business against another in order to drive out competition.²⁶⁴

The Court in *Brown* agreed that section seven reached conglomerate mergers:

[B]y the deletion of the "acquiring-acquired" language in the original text, it hoped to make plain that §7 applied not only to mergers between actual competitors, but also to vertical and conglomerate mergers whose effect may tend to lessen competition in any line of commerce in any section of the country.²⁶⁵ (Footnotes omitted.)

The Court reiterated this in *Procter & Gamble*, where it said that "[a]ll mergers are within reach of §7, and all must be tested by the same standard, whether they are classified as horizontal, vertical, conglomerate or other."²⁶⁶

In *Brown*, it was argued that there was competition in the shoe industry at both the manufacturing and retail levels. The Court, however, refused to accept the argument because the trend in the industry was toward oligopoly.²⁶⁷ Although here the Court was referring to a particular market, it went on to say that

not only must we consider the probable effects of the merger upon the economies of the particular markets affected but also we must consider its probable effects upon the economic way of life sought to be preserved by Congress. . . . Where an industry was composed of numerous independent units, Congress appeared anxious to preserve this structure.²⁶⁸

While the Court recognized that there were some definite advantages to bigness, it felt that Congress had made its choice: "Congress appreciated that occasional higher costs and prices might result from the maintenance of fragmented industries and markets. It resolved these competing considerations in favor of decentralization. We must give effect to that decision."²⁶⁹

In 1966, in *United States v. Von's Grocery*,²⁷⁰ the Supreme Court again addressed itself to the problem of the small businessman being squeezed out by increasing concentration. Mr. Justice Black, tracing the history of the nation's

263 95 CONG. REC. 11498 (1949).

264 *Id.* at 11496.

265 370 U.S. 294, 317 (1962).

266 *FTC v. Procter & Gamble Co.*, 386 U.S. 568, 577 (1967).

267 370 U.S. 294, 333 (1962).

268 *Id.*

269 *Id.* at 344.

270 384 U.S. 270 (1966).

antitrust laws, observed that "[f]rom this country's beginning there has been an abiding and widespread fear of the evils which flow from monopoly — that is the concentration of economic power in the hands of a few."²⁷¹ When earlier acts failed to achieve this end, he noted, the Congress, in 1950, passed the Celler-Kefauver Act, the purpose of which "was to prevent economic concentration in the American economy by keeping a large number of small competitors in business."²⁷² Since the number of small grocery companies in Los Angeles was declining, the merger was held illegal, even though, as Mr. Justice Stewart pointed out in dissent,

[t]he actual market share foreclosed . . . was thus slightly less than 1% of the total grocery store sales in the area. The share of the market preempted by the present merger was therefore practically identical with the 0.77% market foreclosure accepted as "quite insubstantial" by the Court in *Tampa Electric v. Nashville Coal Co.*, 365 U.S. 320, 331-333.²⁷³

Donnem observes that in *Tampa* "there was no particular evil involved, and therefore the low market percentage was insufficient for illegality."²⁷⁴ From this he argues that where there *are* competitive evils involved (as the increasing concentration in *Von's Grocery*), a smaller showing of impact will suffice.²⁷⁵ In *Brown Shoe*, the Court seems to support this view:

[I]t becomes necessary to undertake an examination of various economic and historical factors in order to determine whether the arrangement under review is of the type Congress sought to proscribe.

A most important such factor to examine is the very nature and purpose of the arrangement.²⁷⁶ (Footnotes omitted.)

In *Tampa*, there was no substantive evil involved; the firm was merely trying to assure a steady supply of coal. In *Von's Grocery*, however, there was a competitive evil involved, and therefore little market impact was required.²⁷⁷

Donnem summarizes by saying that

as the evidence concerning qualitative evil to our economic way of life increases, the need to show other anticompetitive elements decreases. Similarly, as the evil of aggregate concentration goes up, the need to show specific impact on business rivalry goes down.²⁷⁸

It is possible, under section seven, to dispense with more rigid market tests because the test is one of incipency: "the amended statute was directed only at mergers after which there would be a reasonable probability of anticompetitive effects."²⁷⁹ This test is met "by an evidentiary showing that provides what the

271 *Id.* at 274.

272 *Id.* at 275.

273 *Id.* at 296 (dissenting opinion).

274 R. Donnem, *supra* note 251, at 55,578.

275 *Id.* at 55,580.

276 370 U.S. 294, 329 (1962).

277 See *Fortner Enterprises, Inc., v. United States Steel Corp.*, 394 U.S. 495 (1969) (little market impact was found, yet the arrangement was held illegal).

278 R. Donnem, *supra* note 251, at 55,580.

279 Turner, *supra* note 29, at 1316.

Justices consider to be adequate support for predicting that in the future the impact on competition will be somewhat more than *de minimis*.²⁸⁰ In *Brown Shoe*, the Court rejected a Sherman-type standard and instead embraced the view that Congress'

concern was with probabilities, not certainties. Statutes existed for dealing with clear-cut menaces to competition; no statute was sought for dealing with ephemeral possibilities. Mergers with a probable anticompetitive effect were to be proscribed by this Act.²⁸¹ (Footnote omitted.)

Under an incipency test, evidence of a trend toward concentration reduces the need for further evidence.

While past decisions have all rested on market concentration rather than on aggregate concentration, the Court, in light of the legislative history of section seven, could easily expand the coverage of this new merger threat.

Not all people are satisfied by the legislative history approach that the Supreme Court has followed. Turner contends that "[i]n light of the bitterly disputed issues involved, I believe that the courts should demand of Congress that it translate any further directive into something more formidable than sonorous phrases in the pages of the Congressional Record."²⁸²

Northwest Industries argues that even under this approach "[t]he legislative history . . . while indicating serious concern over increases in over-all concentration of manufacturing assets, gives no indication of any intent to deal with concentration directly, nor to declare it illegal."²⁸³

While it is true that Congress did not declare it illegal,

recognition of this is little or no defense for the continuation of mergers. The clear expression of purpose in the Senate report indicates that the proposed antimerger bill "is to limit future increases in the level of economic concentration resulting from corporate mergers and acquisitions." Thus it is the method of gaining bigness that is being attacked.²⁸⁴

Northwest's argument that there must be "probable and substantial anti-competitive consequences in one or more sections of the country"²⁸⁵ deserves closer attention. As the government put the question, "[w]hat is at stake is whether Section 7 can reach mergers whose impact is *not* immediate and perceivable in discrete markets like household bleach, shoe retailing"²⁸⁶ It felt that section seven could reach such mergers, because "Congress meant the phrase to be expansive: 'anywhere at all.' Viewed in this light, it was not intended to be, and need not be, an obstacle to the approach we urge."²⁸⁷

Before 1966, there had been a great deal of confusion as to the meaning of

280 R. Donnem, *supra* note 251, at 55,579.

281 370 U.S. 294, 323 (1962).

282 Turner, *supra* note 29, at 1395.

283 Brief in Opposition to Plaintiff's Motion for Preliminary Injunction at 9, *United States v. Northwest Indus., Inc.*, 1969 Trade Cas. ¶ 72,853 (N.D. Ill. 1969).

284 Thomas, *Conglomerate Merger Syndrome — A Comparison: Congressional Policy with Enforcement Policy*, 36 *FORD. L. REV.* 461, 540 (1968).

285 Brief in Opposition, *supra* note 283, at 10.

286 Plaintiff's Answer, *supra* note 91, at 25.

287 *Id.* at 23.

the phrase "in any line of commerce in any section of the country." The Supreme Court had said that "[d]etermination of the relevant market is a necessary predicate to a finding of a violation of the Clayton Act because the threatened monopoly must be one which will substantially lessen competition 'within the area of effective competition.'"²⁸⁸ The dispute arose over how the "lines" were to be drawn.

In 1961, two commentators felt that

decisional law has now developed to the point where several propositions can be asserted:

(1) Definition of the relevant market or "line of commerce" in a Section 7 proceeding is not an idle pastime; it is the threshold question and a "necessary predicate" to any finding of violation, since anticompetitive effects can be measured only within a market framework.

(3) The permissible range of substitute products is not infinite, and the test is not designed to embrace "inter-industry" competition; but it does allow for the inclusion of more than one product in the same market if they are effectively competitive.²⁸⁹

With the decision in *Brown Shoe*, the beginnings of change were evident. In August, 1962, shortly after the decision was handed down, the American Bar Association Section of Antitrust Law held a panel discussion in San Francisco to discuss the implications of *Brown*. During the discussion, George Reycraft said that "the Court has left open for the government a very great degree of latitude in picking the lines of commerce, and I think from that standpoint, wherever the two companies involved compete, that is going to be close to being the line of commerce."²⁹⁰

This reasoning received a boost in the 1966 *Pabst Brewing* case.²⁹¹ The Court said that the district court had erred in thinking that

in order to show a violation of §7 it was essential for the Government to show a "relevant geographic market" in the same way the corpus delicti must be proved to establish a crime. . . . [I]t must . . . prove no more than that there has been a merger between two corporations engaged in commerce and that the effect of the merger may be substantially to lessen competition or tend to create a monopoly in any line of commerce "in any section of the country." The language of this section requires merely that the Government prove the merger may have a substantial anticompetitive effect somewhere in the United States The Government may introduce evidence which shows that as a result of a merger competition may be substantially lessened throughout the country, or on the other hand it may prove that competition may be substantially lessened only in one or more sections of the country.²⁹²

Since the word "any" is used in describing both "line of commerce" and

288 United States v. Du Pont & Co., 353 U.S. 586, 593 (1957).

289 Handler & Robinson, *supra* note 4, at 325.

290 AMERICAN BAR ASSOCIATION, SECTION OF ANTITRUST LAW, SUBCOMMITTEE OF SECTION 7 OF THE CLAYTON ACT, IMPLICATIONS OF *Brown Shoe* FOR MERGER LAW AND ENFORCEMENT 40 (1962).

291 United States v. Pabst Brewing Co., 384 U.S. 546 (1966).

292 *Id.* at 549.

"section of the country," it can hardly be argued that it should be accorded different meanings in describing the two phrases. The Court said that "Congress did not seem to be troubled about the exact spot where competition might be lessened; it simply intended to outlaw mergers which threatened competition in and *or all* parts of the country."²⁹³ (Emphasis added.) In light of *Pabst*, it is difficult to accept the contention of Northwest that

[t]o generalize and treat all of American business or all of American manufacturing as, in effect, a "line of commerce" is not to expand upon or adapt existing principles but to repudiate them completely, in favor of a generalized concept that "bigness" in and of itself is bad and must be thwarted.²⁹⁴

Using the statutory terms, as construed in *Pabst*, the government need only prove that competition may be lessened "in any or all" lines of commerce. The government cannot be faulted, therefore, for arguing that a merger that will tend to decrease competition within the economy as a whole may be prevented by a suit under section seven.

V. Conclusion

In light of the economic climate in 1970 America, it is easy to understand the conglomerate phenomenon; as Textron's Miller put it: "The new technology has created insecurity for single-product companies. They are asking themselves: 'Will we be O.K. 10 years from now — or don't we need to get into some of these new fields?'"²⁹⁵ Narver recognized that there are numerous legitimate reasons why conglomerate-type expansion may be sought:

Market saturation or lack of market growth relative to supply may lead a firm to expand in new directions. Intensified competition in one or more of the firm's markets may make expansion in those markets feasible only by expensive selling efforts and acceptance of lower profit margins.²⁹⁶

A patent expiration may make a previously restricted area very attractive. A company with a cyclical business may wish to expand in a way that would eliminate its seasonal fluctuations. This may also be accompanied by increased opportunity for innovative management:

Our motivation has been to create an option to translate the new technology into useful production, an option to participate in new markets for products that haven't even been designed, and a balanced participation in growth areas so that we are not subject to wide fluctuation.²⁹⁷

Because of the cyclical operations of some of its components, the conglomerate may stagger at times when one company hurts, but what would have happened

293 *Id.*

294 Brief in Opposition, *supra* note 283, at 7.

295 U.S. NEWS & WORLD REP., Oct. 28, 1968, at 79.

296 J. NARVER, *supra* note 95, at 65.

297 U.S. NEWS & WORLD REP., Oct. 28, 1968, at 80.

had the stumbler been on its own? Perhaps the business might even have failed, thus reducing competition.

Expansion may also be sought to absorb excess capacity, thus taking full advantage of possible efficiencies. New geographic markets may open up. Expansion by merger in the company's present area of business may leave the firm open to an antitrust suit. While, admittedly, many of these reasons apply equally to growth through internal expansion, there is no antitrust law that forbids mergers when internal expansion could be used. Only anticompetitive mergers are forbidden; procompetitive practices are not required.

By a flat merger prohibition, we would only increase what Galbraith calls "the element of charade in the antitrust laws. If a firm is already large it is substantially immune under the antitrust laws."²⁹⁸ Would it be just, or even wise, to slap a complete ban on mergers and limit the size of new companies? Rather than a per se rule of illegality for all conglomerate mergers, a rule of reason seems to be the answer. As Willard F. Rockwell, Jr., said:

you can't totally condemn a basic economic trend because of some of its unwholesome by-products. The problem today is to sort out all the aspects of the merger trend and encourage what is healthy, creative and profit-making — and reject the rest.²⁹⁹

The Neal Report suggested action somewhat less drastic than an absolute prohibition of mergers by large firms, opting instead for new legislation which would embody a "leading firm rule" "forbidding mergers between very large firms and other firms that are already leading firms in concentrated markets significant in the national economy."³⁰⁰ In order to effect this policy, the Task Force provides sample legislation setting forth the various prohibitions;³⁰¹ unfortunately, however, the proposed statute falls victim to the defect inherent in any such rule. The Task Force, as it must, offers fixed dollar amounts to delimit the terms "large firm" and "significant market."

By establishing rigid and inflexible monetary guidelines, such a system, especially in time of inflation, is immediately dated: In 1940, the SEC proposed such a system in dealing with regulation of the mutual fund industry, urging an asset limitation of \$150 million.³⁰² The regulation was never adopted, at least in part because it was felt that the companies would never get that large;³⁰³ as of December 31, 1967, only twenty-eight years later, sixty-one domestic mutual funds had attained this then-unbelievable figure, having total net assets in excess of \$150 million, with ten of these having net assets in excess of \$1 billion.³⁰⁴ By establishing similar monetarily defined limits, the proposed statute would soon become an anachronism.

²⁹⁸ Galbraith, *The New Industrial State*, 1 ANTITRUST L. & ECON. REV., Winter, 1967, at 11, 15.

²⁹⁹ U.S. NEWS & WORLD REP., May 19, 1969, at 70

³⁰⁰ Antitrust & Trade Regulation Report No. 411 at 8 (May 27, 1969) [hereinafter cited as NEAL REPORT].

³⁰¹ *Id.* at 15-16.

³⁰² Survey, *The Mutual Fund Industry: A Legal Survey*, 44 NOTRE DAME LAWYER 732, 806 (1969).

³⁰³ *Id.* at 807.

³⁰⁴ *Id.*

Since it was the goal of the Task Force to "prohibit or discourage mergers most likely to have anticompetitive consequences,"³⁰⁵ it would seem best to obtain a merger rule that would withstand the test of time instead of opting for new legislation, the major advantage of which would be the ease of enforcement.

Nonetheless, the policy behind such a rule is sound, because not all conglomerate mergers are anticompetitive:

A conglomerate merger probably will have little or no anticompetitive effect where both parties are small, are low-ranked firms in their industries, inhabit near-atomistic industries, etc. Conglomerate acquisitions of a low-ranking firm (say, eighth position or lower with less than ten per cent of the market) in a concentrated industry may usually be distinctly pro-competitive, particularly if the acquiring firm has growth objectives which will upset cooperative conditions among the leading firms in the entered industry.³⁰⁶

Similarly, FTC Chairman Weinberger recognizes that "conglomerates may provide a stimulus to competition in several ways." He says,

When a conglomerate makes a "foothold acquisition" by acquiring a small company in a concentrated industry the prospect is that it will build the small company into a more vigorous and healthy competitor, and thus give it the strength to meet the leading firms head-on in the arena of competition.³⁰⁷

Both Turner and Weinberger have also expressed apprehension about an absolute rule that would, as Weinberger said, "insulate an inefficient management from a corporate takeover that would in fact have the effect of adding a spur to competition."³⁰⁸

This, in effect, is the policy which McLaren has sought to implement through a judicious use of section seven; he said: "We only attacked those we felt were anticompetitive under existing law."³⁰⁹ At the recent Senate hearings, McLaren reiterated this and said that he would not attack foothold acquisitions, as they could be procompetitive.³¹⁰ This policy was embodied in the LTV consent decree, wherein the Department of Justice only prohibited future acquisition of companies with assets in excess of \$100 million. While the Justice Department's policies can be easily reconciled with the Neal recommendations, there is greater difficulty with the Stigler Report, which adopted a hands-off policy in regard to conglomerate mergers. This attitude was exemplified by Dr. Ronald Coase, who, in the Working Papers to the Report, argued that it would be best to let "[c]ompetition . . . sort them out."³¹¹ This type of "survival of the fittest" attitude also seems to be proposed by Turner, who sees small businessmen being forced to improve or get out:

305 NEAL REPORT 8.

306 Campbell & Shepherd, *supra* note 123, at 1371.

307 1970 Hearings (testimony of Caspar W. Weinberger).

308 *Id.*; accord, *id.* (testimony of Donald F. Turner).

309 St. Paul Dispatch, Dec. 24, 1969, at 2, col. 6.

310 1970 Hearings (testimony of Richard W. McLaren).

311 Coase, *Working Paper II: The Conglomerate Merger*, 2 ANTITRUST L. & ECON. REV., Spring, 1969, at 45.

To be sure, they may be unable to survive the pressures, and therefore the longrun consequences of entry by a diversified company with substantial cost advantages may be a material change in the structure of the industry concerned. Large, diversified firms may tend to supplant small, single-product companies; and perhaps, though not necessarily, the *number* of sellers may eventually decline.³¹²

This view, however, was repudiated by the Supreme Court:

[W]e cannot fail to recognize Congress' desire to promote competition through the protection of viable, small, locally owned businesses. Congress appreciated that occasional higher costs and prices might result from the maintenance of fragmented industries and markets. It resolved these competing considerations in favor of decentralization. We must give effect to that decision.³¹³

From experience with other merger trends, it is probable that government action will be required to implement this directive. As the Department of Justice contends,

[t]here is good reason to conclude that the trend of mergers among large diversified industrial concerns temporarily slowed by adverse market conditions and perhaps by the Government's enforcement efforts under Section 7, ultimately can be contained only by the law.³¹⁴

Because "[t]he current rate and pattern of mergers is causing significant and apparently permanent changes in the structure of the economy, and the long-run impact of these changes cannot be readily foreseen,"³¹⁵ some immediate action must be taken. The Stigler Report reached an opposite conclusion because of its belief that "[a]lmost by definition such a firm [a conglomerate] poses at most a minor threat to competition."³¹⁶ It consequently "strongly recommend[ed] that the Department decline to undertake a program of action against conglomerate mergers and conglomerate enterprises, pending a conference to gather information and opinion on the economic effects of the conglomerate phenomenon."³¹⁷

The immediacy of the situation, however, neither offers sufficient time nor demonstrates the necessity for going through another lengthy process of conferences, reports, additional congressional hearings, legislation, and court action to test the new legislation. There is already a plethora of case law, articles, and congressional hearings dealing with the traditional concepts of antitrust law which McLaren has merely repackaged under the label of the aggregate concentration theory. The Stigler Report is strictly behind the times when it says:

Antitrust law has seemed to some a convenient weapon with which to attack large conglomerate mergers. If one interprets "elimination of

312 Turner, *supra* note 29, at 1353.

313 Brown Shoe v. United States, 370 U.S. 294, 344 (1962).

314 Plaintiff's Answer, *supra* note 91, at 17.

315 Complaint at 7, United States v. International Tel. & Tel. Corp., Civil No. 13320 (D. Conn., filed Aug. 1, 1969), *prelim. inj. denied*, 1969 Trade Cas. ¶ 72,943.

316 STIGLER REPORT 30.

317 *Id.* at 15.

potential competition," "reciprocity," and "foreclosure" as threats to competition, one can always bring and usually win a case against the merger of two large companies, however diverse their activities may be. These are often makeweights.³¹⁸

These activities, which form the basis of the aggregate concentration theory, have long stood condemned by the Supreme Court as *anticompetitive*. In view of *United States v. El Paso Natural Gas Co.*,³¹⁹ *FTC v. Procter & Gamble*,³²⁰ and *FTC v. Consolidated Foods*,³²¹ it is hard to see how these abhorrent practices can be so easily dismissed. These cases *were* based on economic considerations, just as the Stigler Report recommends.

McLaren has said that "our policy is not designed to penalize success; rather, it seeks to insure that further growth of large firms is legitimately achieved, *i.e.*, without injury to the growth prospects of others, and without damaging the competitive process."³²² To make this policy work, the Stigler Report wisely recommends that economists play a wider role in antitrust enforcement to assure that the remedies devised "will not shatter on economic realities."³²³ It could also be helpful "to institute semi-public conferences to assist in the formulation and frequent reevaluation of enforcement guidelines."³²⁴

McLaren is in agreement with the Stigler Report that antitrust suits must make good economic sense; his policy is to emphasize "the remedial rather than the punitive thrust of civil antitrust proceedings, [because] it removes the conscious or subconscious impediment of moral judgment from the path of an effective enforcement program."³²⁵

The aggregate concentration theory, if accepted by the courts, should do much to remedy the anticompetitive effects of the present merger movement. This would have much the same effect as the proposed "rule of antitrust law, that leading-firm conglomerate mergers are presumptively unlawful under Section 7 of the Clayton Act."³²⁶ It would also fit comfortably within the Neal Report recommendations that "mergers between very large firms and other firms that are already leading firms in concentrated markets significant in the national economy" be forbidden³²⁷ and "that restrictions on mergers should continue to be based on considerations related to competitive market structure."³²⁸

Since the courts have not yet expressed their opinion on the merits of these new conceptual arrangements, it would be unwise to immediately scuttle the present approach in favor of new legislation which would either be couched in the same general terms of the present section seven or in the impracticably pre-

318 *Id.* at 30.

319 376 U.S. 651 (1964).

320 386 U.S. 568 (1967).

321 380 U.S. 592 (1965).

322 R. McLaren, *Looking Ahead in Antitrust*, Address at Northwestern University Law School, Oct. 8, 1969, in 5 CCH TRADE REG. REP. ¶ 50,258, at 55,544.

323 STIGLER REPORT 19.

324 *Id.* at 14.

325 R. McLaren, *supra* note 322, at 55,541.

326 Campbell & Shepherd, *supra* note 123, at 1363. Leading firm conglomerate mergers are defined as "those in which the acquiring and acquired firms are each among the few largest firms in at least one concentrated industry which is large enough to be significant." *Id.*

327 NEAL REPORT 8.

328 *Id.* at 3.

cise terminology suggested by the Neal Report. James Nicholson, former FTC Commissioner, said that

[b]y the enactment of the Celler-Kefauver amendment, Congress declared the national antitrust policy in the merger area. In so doing it left to the courts and enforcement agencies responsibility for filling out and adjusting that general policy in the constantly shifting dynamics of the economy.³²⁹

This was emphasized by FTC Chairman Weinberger, who pointed out that "[u]nless and until the outer limits have been fully explored, it is not possible to say that the existing law is inadequate."³³⁰ McLaren also argued that the present law must be tested before new legislation was presumed to be necessary.³³¹

By strict enforcement of the present section seven, most anticompetitive practices can be attacked and structural market relief can be obtained.

Through such an enforcement program, most of the beneficial effects of conglomerate mergers would be maintained while the dangerous increase in concentration would be halted. This is the type of program that the majority has demanded; it is also the type of program that is now being pursued.

Gerald Grieman

329 1970 Hearings (testimony of James M. Nicholson).

330 *Id.* (testimony of Caspar W. Weinberger).

331 *Id.* (testimony of Richard W. McLaren).