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THE POLITICAL RAMIFICATIONS OF ANTITRUST AND CONGLOMERATE MERGERS

EDWARD SOFEN*

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I. ANTITRUST IN THE BEGINNING

There is no simple way of dealing directly with the question of conglomerate mergers without becoming enmeshed, at least to some degree, in the metaphysical complexities which bear upon the question of whether a substantial share of the market, when considered alone, has a desirable or undesirable effect on the economy. Indeed, as illustrated below, one could have a field day just exploring the peripheral question of the extent of business concentration in the American economy.

Over the years, students of economics have engaged in polemic arguments concerning this question. Some have stressed the fact that concentration was either static, declining, or, regardless of its direction, traveling at the pace of a "glacial drift."¹ One study revealed that big business growth, percentage-wise, merely paralleled the development of the economy as a whole, and that the number of businesses per thousand of the population was greater than ever before.² Moreover, only thirty-six of the 100 largest companies in 1948 held top-ranking positions of leadership in 1909; the remaining sixty-four had climbed to such heights only within the last twenty years.³ If this theory is valid, however, position in the area of concentration might be as tenuous as class or social status.

The adherents of another school of thought, fortified by a plethora of private and governmental sources, looked upon a glacier as dangerous no matter at what speed it was travelling. Others went so far as to declare that American business had reached the highest degree of economic concentration in history. If one examined the entire economy, less agricultural production, it appeared that 500 corporations owned two-thirds

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3. Id. at 141-43.
of all the productive assets. Professor Adolph Berle, whose statistics have been quoted above, concluded that "these 500 groupings—each with its own little dominating pyramid within it—represent a concentration of power over economics which makes the medieval feudal system look like a Sunday School party."

During the economic concentration hearings of 1965, it was indicated that between 1950 and 1962 the share of manufacturing assets held by the 200 largest corporations had increased from 46.7 percent to 54.6 percent, and the market share of the 100 largest firms had grown from 38.6 percent to 45 percent. Put somewhat more dramatically, the share of the market held by the 100 largest companies in 1962 was almost equal to the share held by the 200 largest in 1950.

Still another classic statistic relating to the extent of merger activity since 1950 is that acquisitions by the 200 largest manufacturing companies eliminated over 2,000 concerns with combined assets of about 17.5 billion dollars.

The power of the corporation cannot be assessed exclusively in statistical terms, nor is it the purpose of this writer to become involved in a hassle with the magicians of the slide-rule. Quantitative measurements too frequently embrace everything but the soul and the spirit. To fully appreciate the dilemma confronting the political economist in assessing the role of bigness today, it would seem advisable to examine, at least briefly, the metamorphosis of the philosophy of the Sherman Act as it affects or might affect mergers.

The "triumph of American capitalism" was manifested in the last decades of the 19th Century and the early decades of the 20th Century by the birth of great mergers of corporations such as Standard Oil, U.S. Steel, American Tobacco, and International Harvester. One student of the legislative history of the years immediately preceding the enactment of the Sherman Act concludes that "there were few who doubted that the public hated the trusts fervently." The public insisted upon a remedy which would destroy the power of the trust before it engulfed everything in sight. Among the evils for which the trusts were condemned were the corruption of the administrative agencies, the increase in consumer prices, the watering of stock, the closing down of plants, the manipulation of tariffs, and the jeopardizing of employment. The Republican Party, as the alleged party of the "rich" and the "monopolists," felt an even greater compulsion than the Democrats to condemn trusts. A banquet given for the Republican Presidential candidate by a distinguished group of businessmen which included Messrs. Gould, Vanderbilt, and

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Astor, was described by The New York World as “the Royal Feast of Belshazzar Blaine and the Money Kings” during which the “Millionaires and the Monopolists” pledged their mutual allegiance to the party. It was a Republican, however, who subsequently initiated the antitrust act which was to bear his name. Senator John H. Sherman intended the act to include within its jurisdiction the great industrial trusts, mergers, tight combinations, and even certain kinds of loose combinations which tended to prevent full and free competition. Mr. Sherman was echoing the sentiment of most of his colleagues who believed that the principle of free competition was so self-evident that there was little need for extended argument on its behalf.

Why then, if these strong views persisted, did not Congress enact a law requiring positive steps toward competition rather than merely legislating against monopoly? The answer can probably be found in the customs of the time and, more particularly, in the precedent for using the common law doctrine of prohibition to combat both restraints of trade and monopoly. The Sherman Act was viewed not as an attack upon the system but rather as a purge of its excesses. Thus, the task of the state was not to impose any artificial set of governing regulations but rather to make certain that the market mechanism could operate freely. The impersonal forces of the market place were believed to possess a built-in morality which automatically would safeguard the best interests of society. How much the businessman ought to charge the consumer for a given product and how much he ought to pay his employees were all matters that could best be answered in terms of his own self-interest. Each man, by pursuing his own selfish ends, would in reality be working towards a selfless goal of a richer and happier society. One, consequently, could have his profits and enjoy an easy conscience. Thus, while the foundations of the laissez-faire government rested upon the individual choice and the free will of the totality of the numerous buyers and sellers, it nevertheless bestowed upon the businessman a “dispensation from responsibility for moral, philosophical, political, and social decisions in economic affairs.” One could no more become indignant with the laws of supply and demand than he could with the laws of gravity.

Possibly the amoral quality of a laissez-faire system may have eased the corporate conscience in its violation of the strictures of the Sherman Anti-trust Act. A far more activist philosophy arising in defense of this “devil take the hindmost” approach towards economic growth and concentration was the gospel of Darwin’s doctrine of “survival of the fittest.” When Herbert Spencer applied the general laws of evolution to the social arena, he provided the philosophical justification for the

8. Id. at 248.
10. Id. at 226.
business tycoons during America’s greatest spurt of trusts. Social Darwinism was made quite popular among the businessmen and their allies by the sale of more than 360,000 copies of Mr. Spencer’s works between the 1860’s and 1900; and this was before the advent of Book of the Month and other such clubs.

It would have been a strange phenomenon for the most powerful economic and political entity of the early 1900’s to have been condemned too severely by the courts. One could hardly have expected the Supreme Court, which had transformed the fourteenth amendment into Herbert Spencer’s Social Statistics, to have been inspired by divine guidance to interpret the Sherman Act in its purest sense as forbidding every contract or monopoly in restraint of trade.

Thus, it came as no surprise that the courts created the dichotomy of good and bad trusts. The mechanism for accomplishing this transition was the “rule of reason.” Mere size in and of itself was not an offense. The “abuse theory of mergers” viewed as evil only those consolidations with an overwhelming percentage control of industry which were engaged in predatory practices or unlawful conduct. Somewhere, in the unfolding of this theory, sight was lost of the evil of all and any kind of monopoly power exerted or unexerted.

Another less explicit, but still implied meaning of the Sherman Act, also slighted by the court, was Justice Brandeis’ belief that the “curse of bigness,” standing alone, is a menace to society. The courts, in expounding the rule of reason with its emphasis on intent and practices, made irrelevant the concept of either market control or monopoly power. “The distinction between good and bad trusts” as observed by Professor Milton Handler, “belongs to that outmoded era when the anti-trust laws were regarded as a moral pronouncement rather than a charter of economic freedom.”

II. THE NEW SHERMAN ACT

With the advent of the great depression and the mounting evidence of such big business phenomena as concentration, separation of ownership and management, price leadership, and the basing point system, the cultural lag between 19th Century theory and 20th Century practice became evermore apparent. The “TNEC” hearings and a postdepression school of scholars challenged the shibboleth of classical competition

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in modern society and warned against the dangers that the monopoly posed to democratic institutions. Writer after writer expressed the fear that the power of business not only competed with that of the state but threatened to absorb the state. Robert A. Brady, a professor of economics, warned that “sovereign power is indivisible, and a house cannot long remain divided against itself.” Stephen Raushenbush, author, businessman, and government administrator, believed that the modern corporation’s desire to keep the state weak might beget the seeds for the growth of Fascism, Nazism, or Communism. Charles Beard, the well-known historian, presaged President Eisenhower’s warning against the growth of the military-industrial complex.

If the advocates of this school of thought feared bigness as a threat to democracy, they looked for salvation to the “diffusion of power among the people.” “Unless ‘we the people’ can make the industrial system the instrument of the general welfare, the dominant interests will take over the government. For the separation of state and economy is now gone.”

A. Unexercised Monopoly Power as a Violation

The United States Supreme Court reflected at least some of these views in its new interpretation of the Sherman Antitrust Act. A new Sherman Act emerged from the Alcoa case in 1945. Acting as a court of last resort, the Second Circuit Court threw out the abuse theory of mergers and held that Alcoa did in fact possess a monopoly of the aluminum industry in the United States in violation of section 2 of the Sherman Act despite the absence of any predatory practices. Judge Learned Hand wondered how it could be possible for price-fixing arrangements to be illegal per se, whereas, a single monopoly firm which eliminated all competition, including that of price, was not. Necessarily, when a monopoly did fix a price, it would have to fix a price of its own choice for “the power and its exercise must needs coalesce.” Thus, the doctrine postulated in the earlier cases that the existence of unexerted power was no offense was substantially weakened.

The Alcoa court also dealt with the question of specific intent to

16. Adolph A. Berle, Jr., Robert A. Brady, Robert S. Lynd, Stephen Raushenbush and a number of others share a common set of views that might be characterized as a school of thought.
20. Lynd, Foreword to R. BRADY, supra note 17, at viii.
22. United States v. Aluminum Co. of America, 148 F.2d 416 (2d Cir. 1945). When the Supreme Court could not secure a quorum, the case was referred to the Court of Appeals in the second circuit as the court of last resort.
23. Id. at 428.
monopolize and held that "no monopolist monopolizes unconscious of what he is doing." Judge Hand further opted for competition on grounds similar to those advocated during the debate over the enactment of section 7 of the Clayton Act. He went on to say:

Many people believe that possession of unchallenged economic power deadens initiative, discourages thrift and depresses energy; that immunity from competition is a narcotic, and rivalry is a stimulant, to industrial progress; that the spur of constant stress is necessary to counteract an inevitable disposition to let well enough alone. Such people believe that competitors, versed in the craft as no consumer can be, will be quick to detect opportunities for saving and new shifts in production, and be eager to profit by them . . . . True, it might have been thought adequate to condemn only those monopolies which could not show that they had exercised the highest possible ingenuity, had adopted every possible economy, had anticipated every conceivable improvement, stimulated every possible demand . . . . Be that as it may, that was not the way that Congress chose; it did not condone "good trusts" and condemn "bad" ones; it forbade all. Moreover, in so doing it was not necessarily actuated by economic motives alone. It is possible, because of its indirect social or moral effect, to prefer a system of small producers, each dependent for his success upon his own skill and character, to one in which the great mass of those engaged must accept the direction of a few. These considerations, which we have suggested only as possible purposes of the Act, we think the decisions prove to have been in fact its purposes.

The views enunciated by Judge Hand in the Alcoa case were echoed by the United States Supreme Court in American Tobacco Company v. United States. In American Tobacco, intent was inferred from the identity of price behavior, and "neither proof of exertion of the power to exclude nor proof of actual exclusion of existing or potential competitors" was necessary to sustain a charge of monopolization under the Sherman Act. All that was required to prove the crime of monopolization under section 2 was "that power exists to raise prices or to exclude competition when it is desired to do so." The Court raised the issue of large advertising expenditures, which was to play such an important role in later years in cases involving conglomerate mergers. The Court stated:

Such tremendous advertising, however, is also a widely published warning that these companies possess and know how to use a powerful offensive and defensive weapon against new com-

24. Id. at 432.
25. Id. at 427.
27. Id. at 810.
28. Id. at 811.
petition. New competition dare not enter such a field, unless it be well supported by comparable national advertising. Prevention of all potential competition is the natural program for maintaining a monopoly here, rather than any program of actual exclusion.  

A few years later, in United States v. Griffith, the monopolization issue was further elaborated upon by Mr. Justice Douglas. As in the previous cases, it was held that specific intent was not necessary to prove monopoly—it was sufficient that restraint of trade or monopoly was a consequence of the defendant's conduct. Justice Douglas concluded that section 2 was aimed at the acquisition or retention of effective market control and that "monopoly power, whether lawfully or unlawfully acquired, may itself constitute an evil and stand condemned under § 2 even though it remains unexercised."  

Despite these enlightened views of the Sherman Act, court decisions, until 1962, substantially ignored the concept of oligopoly power. The frame of reference for the Sherman Act remained monopoly not oligopoly. As Mr. Joseph F. Brodley observed, "even the vocabulary of anti-trusts failed. Prices were not fixed but administered. Conditions of scale were not dictated by monopoly combine but set by a price leader." Mr. Brodley contends that anti-trust met its greatest defeat because it failed to cope with oligopoly power.  

To be sure, there had been some passing reference to oligopoly power in the "doctrine of parallel action" as it was applied to section 1 of the Sherman Act, and also in the "identity of behavior" and "concert of action" policies as they were applied to section 2 of the Act. However, the principle that emerged in the handful of cases referred to above atrophied through disuse.

B. The New Competition

With the advent of prosperity and affluence in the post World War II period, the fears of the postdepression school seemed highly imaginary. Yet, the fact remains that many of the views expressed by this group, such as the diffusion of power theory, were a fundamental part of American beliefs and mythology. By the 1950's, the time had arrived for a new school of thought to emerge and attempt to salvage some of the old basic values and make them compatible with the realities of economic

29. Id. at 797.
30. 334 U.S. 100 (1948).
31. Id. at 107.
33. Id. at 289.
concentration. John K. Galbraith, David E. Lillienthal, and Adolph A. Berle, Jr., each of whom might be characterized as a liberal, or, at least, a realistic liberal (which is not necessarily a contradiction in terms) brought forth a new theory of competition. Under this new idea, capitalism was not doomed; it had more vitality than ever. The classical model of competition with its numerous buyers and sellers had been abandoned, but in its place had emerged new competing forces as contemplated by the Schumpeterian dialectic. Thus was born a new theory of competition based upon substitute products, research, better and more efficient managerial techniques, public relations consciousness, creative destruction, and most important of all, the rise of the countervailing powers. Decisions as to prices, wages, expansion of plant and output would, like Adam Smith's "invisible hand", now be dependent upon the competition of economic forces beyond the businessman's control. Despite the fact that there was the same apparent inevitability in the empirically verified growth of countervailing powers, as there was to be found in the laws of supply and demand, Mr. Galbraith appeared to be unwilling to place his complete reliance upon the automatic self-generation of such forces. He added this qualifying thought:

In the light of the difficulty in organizing countervailing powers, it is not surprising that the assistance of government has repeatedly been sought in this task. Without the phenomena itself being fully recognized, the provision of state assistance to the development of countervailing power has become a major function of government—perhaps the major domestic function of government today.

There is the additional argument of the new school that it is in the nature of the modern state that the business manager is himself a pluralistic personality. By this interpretation, he is conceived as being quite different from his prototype of the past. He is depicted essentially as a professional man trained in the schools of business administration of some of our most enlightened colleges and universities. Because his managerial decisions must be made with an eye to public opinion, he lives in a political milieu similar to that of a politician and public administrator. Consequently, the argument is made that he may rise above the provincialism of his constituents and see himself as a trustee for the nation at large. Such an outlook, it is contended, makes him competent to assess public opinion.

How does one recognize this new deity—"public opinion"—particularly if it is in that state of metamorphosis where it is still uninformed,

38. D. Lillienthal, Big Business (1953).
40. J. Galbraith, supra note 37, at 133.
inarticulate, and incapable of resisting manipulation in any one of a number of directions? Professor Berle, who conceived of the "corporate soul," is not convinced that it can be saved by the ministrations of the high priests of public relations, who are "commonly more royalist than the king. . ." The idea of the businessman as a trustee of society is not new and actually reached a high degree of theoretical development under the Japanese Zaibatsu, the Nazi industrialist, and the old Rockefeller interests in this country. The trustee philosophy advocated for the managers of the various public and quasi-public corporations is, of course, not analogous to the private overlord, for the professional manager does not exist as a power unto himself. The governor, the secretary of agriculture, the president of a union, the pastor of a church, the superintendent of schools—all represent groups with distinctive interests. All too frequently, however, "behind the fiction of the 'manager class' so conveniently sterilized from the taint of special interests stands the same old power. 'The voice is Jacob's voice, but the hands are the hands of Esau.'"

The equilibrium theorists contend that when an imbalance is created in our society, pluralism does provide the equilibrium. This belief is not merely a reflection of hope that man will act rationally and make the necessary adjustments to life; rather, it seeks to establish the principle of equilibrium as a scientific reflex of living. It apparently must work. Such a view of trend and counter-trend or force and counterforce is but a libertarian rendition of thesis, antithesis, and synthesis. It is determinism with a broader base than mere class structure.

Behavior follows belief and belief reflects theory, however vague or profound the comprehension of the theory may be. Doctrinal shifts filter down slowly from learned journals and the exchange of theoreticians, but in the end they have an effect.

C. Innocent Monopoly

A series of cases emerging after 1950 appeared to accept some of the implications of the new competition. In this respect, it may be rather revealing to further examine the ramifications of the Alcoa case. The "new critics" of antitrust took Judge Hand to task for suggesting that Congress had not been motivated by economics alone. They argued that the emphasis on social purpose is generally a smoke screen—a kind of compensation for a guilt complex—that is used whenever the application

42. R. Brady, supra note 17, at 260.
43. R. Lynd, Foreword, supra note 20, at XVI.
of the Sherman Act seems to countenance anti-efficiency. To these observers, the idea that the law prefers the preservation of small businesses to a free market is of dubious validity as a social policy and impossible of application as an antitrust doctrine. Coexistence between the social policy argument and the procompetitive rules can only create a guessing game which is hardly deserving of being known as a system of law.

An examination of the Alcoa case reveals that Judge Hand’s decision was neither as pure nor as simplistic as his critics avowed. Judge Hand pointedly observed that, “a single producer may be the survivor out of a group of active competitors, merely by virtue of his superior skill, foresight, and industry.” For these and other reasons which could automatically or accidentally lead to monopoly, the court believed that a strong argument could be made that the Sherman Act did not condemn the result of such forces, even when the public might be exposed to the evils of monopoly. Furthermore, Judge Hand’s dictum, that over 90% market control was a clear monopoly, 64% doubtful, and 33% clearly not, shows that he was hardly obsessed with the preservation of small business. Apparently, Judge Hand saw no aberration in the existence of oligopoly.

Judge John C. Knox, when faced with the problem of applying the Alcoa case to a much changed postwar economy, pried wider the opening made by Judge Hand and, in doing so, further elaborated upon the views of the new competition. There were certain relevant factors according to Judge Knox that determined the extent of permissible power consistent with the antitrust laws: the number and strength of firms in the market; effective size from a technological and competitive standpoint; the availability of substitute materials; foreign trade; national security interests in the maintenance of strong productive facilities; and maximum scientific research and development. These factors were to be considered together with the public interest in lower costs and uninterrupted production. The rationalizations of the court were that aluminum was a public necessity, that it was in fierce competition with other products, that bigness was an actuality, that trade rivals must be of comparable strength, and that companies must be able to compete with producers of substitute products.

By 1950, as a result of the actions of the War Assets Administration, two competing companies, Kaiser and Reynolds, were added to the aluminum industry. Judge Knox’s decree in United States v. Aluminum Co. of America, required the shareholders of Alcoa to dispose of their stock interests either in that company or in Aluminum Limited of Canada, which was controlled by the same nine stockholders as the Aluminum Company of America. Grant-back provisions of patent licenses

46. United States v. Aluminum Co. of America, 148 F.2d 416 (2d Cir. 1945).
48. Id.
49. Id.
executed by Alcoa with other aluminum companies were declared invalid, and the court retained jurisdiction for another five years of action against Alcoa under the Sherman Act, should the need arise for additional relief.

The government's request that the parent company, Alcoa, be divided into two separate but not equal-sized entities, one of which would become independent of Alcoa, was denied. The court was concerned that dividing the personnel and equipment would impair Alcoa's research and management functions and would constitute a singular disservice to the public. Moreover, the financial benefits received by Kaiser and Reynolds, through the government's war disposal program, would place a new company at a decided disadvantage.50

In his learned opinion in the United Shoe Machinery case,51 Judge Charles Wyzansky gave further support to the doctrine that monopoly was legal if it was "thrust upon" the monopolist. The evidence showed that United controlled the market and that such control could not be attributed entirely to such excusable causes as "the result of superior skill, superior products, natural advantages, technological or economic efficiency, scientific research, low margins of profit maintained permanently, and, without discrimination, legal licenses, or the like."52 There were other barriers, however, such as leasing and exclusive long term contracts which were erected by United's own business policies. Although not illegal in and of themselves, these policies, when applied by a dominant firm like United, operated to exclude competitors. Thus, monopoly was acceptable if attained only by economically superior methods. The decision was affirmed per curiam by the United States Supreme Court,53 and a new concept of "good" and "bad" monopolies had been born with the assistance of midwives Hand, Knox, and Wyzansky.

The courts in dealing with combinations and monopoly still seemed to be more concerned with alleged economic efficiency than with the purported purpose of the Sherman Act as a "charter of liberty" concerned with the diffusion of power.

III. Section 7 of the Clayton Antitrust Act and the Prohibition of Mergers

Clair Wilcox succinctly summarized the main differences between sections 1 and 2 of the Sherman Act and section 7 of the Clayton Act when he observed the following:

The Sherman Act, in its application to combinations, was punitive and corrective. Section 7 of the Clayton Act was designed to be preventive. The test of illegality in the Sherman Act was

50. Id. at 417-19.
52. Id. at 297.
strict: it required proof of accomplished monopolization or of intent to monopolize. The test in the Clayton Act was easier to meet: it required only a reasonable probability that competition would be substantially lessened at some future time. Convictions should thus have been easier to obtain under the Clayton than under the Sherman Act. But here, again, judicial interpretation robbed the law of force.\textsuperscript{54}

Prior to the enactment of the Clayton Act in 1914, mergers had been confined primarily to corporate acquisitions of stock in competing enterprises. The original section 7 of the Clayton Act provided that

\begin{quote}
no corporation engaged in commerce shall acquire . . . the whole or any part of the stock . . . of another corporation . . . where the effect of such acquisition may be to substantially lessen competition between the corporation whose stock is so acquired and the corporation making the acquisition, or to restrain such commerce in any section or community, or to tend to create a monopoly in any line of commerce.\textsuperscript{55}
\end{quote}

Ingenious corporation lawyers soon discovered an escape hatch in the absence in the Act of any prohibition against the acquisition of the assets of a competing firm. Court decisions contributed to the decline of section 7 by holding that the Commission was powerless to ban a merger so long as a company used its stock purchases to acquire the assets before the Commission had acted.\textsuperscript{56} The result was that section 7 was rendered impotent and that acquisition of assets became the name of the game.

To remedy these deficiencies of section 7, to strike down mergers beyond the reach of the Sherman Act, and to cope with what Congress believed to be the steadily upward level of concentration brought about in considerable part by mergers, acquisitions and consolidations, section 7 was amended by the Celler-Kefaufer Act in 1950.\textsuperscript{57} To be sure, the transformation of section 7 into a potent weapon for merger control could not undo the concentration which had already occurred under the Sherman Act.\textsuperscript{58} However, \textquoteleft\textquoteleft the intent here, as in other parts of the Clayton Act, [was] to cope with monopolistic tendencies in their incipiency and well before they have obtained such effects as would justify a Sherman Act proceeding . . .\textquoteright\textquoteright There was no question but that section 7 was meant to reach far beyond the Sherman Act.

\textsuperscript{58} Asch, \textit{Public Merger Policy and the Meaning of Competition}, 6 \textit{Q. Rev. of Econ. & Bus.} 53, 54 (1966) [hereinafter cited as Asch].
\textsuperscript{59} S. Rep. No. 1775, \textit{supra} note 55, at 4-5.
The Federal Trade Commission in 1948 had warned that in respect to the national scene the end does not seem to be in sight unless "like Alexander the Great, the modern monopolist may have to bring his merger activities to a halt owing simply to the imminent absence of 'New Worlds to Conquer.'"\(^6\) The Commission warned that if nothing was done to check the growth of concentration, either the giant corporations would take over the country or government itself would be impelled to resort to direct regulation.\(^6\) Derek C. Bok and others are somewhat contemptuous of the faulty conclusions of the 1948 Federal Trade Commission Report and of the unknowledgeable rhetoric, the economic naiveté, and the singlemindedness with which the proponents of the amended section 7 pursued their twin obsessions of concentration and mergers. Mr. Bok concludes that the "situation was appraised in the same Jeffersonian egalitarian fashion by almost all who spoke for the bill."\(^6\) The latter observation represents to some economists the cardinal sin of attempting to analyze profound economic problems in the simplistic terms of what Schumpeter referred to as "sheer ideology."\(^6\) However, Mr. Schumpeter made no pretense that he believed democratic processes could do anything meaningful about large firms in particular or business practices in general. To the economic sophisticates, it appears most unfortunate that the courts cannot cavalierly ignore the intent of the framers, but for them there is still the saving grace that "this is not to say that every legislative misconception must be rigorously applied until it is formally retracted."\(^6\) One may indeed breathe a sigh of relief that "legal requirements are prescribed by legislators and courts, not by economic science."\(^6\) To be sure, economic theory does provide the courts with a tool for analysis but it does not (if this author may be so bold as to borrow the economic terminology of competition) provide a "workable" or "effective" standard of legality, particularly when applied to future behavior. One should take note of the virtually impossible task which the court, or for that matter any body of reasonable men, must encounter when considering in its totality the complex and illusive economic data that is relevant in cases involving the effects of mergers.\(^6\) Professor Donald F. Turner, who devastatingly casts doubt upon many of the economic arguments for the voiding of mergers, nevertheless still concludes that a Pandora's box would be opened if the outcome of cases

61. *Id.* at 68.
63. Mason, Schumpeter on Monopoly and the Large Firm, Rev. of Econ. & Statistics 139-44 (1951).
64. Bok, *supra* note 62, at 234.
depended upon the review of all the conceivable economic facts.\textsuperscript{67} These admonitions hardly reflect anti-intellectual overtones. It would seem to this observer, that the court is in no position to launch esoteric missiles into economic outer space if it is to cope with the earthy problems that confront it in its case by case approach.

In a unanimous decision in \textit{Brown Shoe Co. v. United States}, the Supreme Court interpreted the amended section 7 for the first time.\textsuperscript{68} In banning a merger in a fragmented industry which would have given Brown, a manufacturer as well as a retailer, about 7.2\% of the nation's retail shoe stores and 2.3\% of the nation's total retail shoe outlets, the Court was concerned with the tendency to establish a precedent which would further the type of oligopoly that Congress had sought to avoid.

We cannot avoid the mandate of Congress that tendencies towards concentration in industry are to be curbed in their incipiency, particularly when these tendencies are being accelerated through giant steps striding across a hundred cities at a time. In the light of the trends in this industry, we agree... that this is an appropriate place at which to call a halt.\textsuperscript{69}

The Court acknowledged that some benefits might accrue to the consumer from the economics of scale resulting from the merger. Brown's expansion, however, was not illegal merely because the small independent stores might be adversely affected; it was competition, not competitors, with which the Act was concerned. Despite this proviso, the Court went on to add:

\textit{[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.}\textsuperscript{70}

This decision further distinguished between the activities that tended toward concentration or oligopoly and those that were promotive of competition. Thus, it held that Congress had not intended to prevent a merger of two small companies if this would enable them to more effectively compete with the dominant firms.\textsuperscript{71}

Still another development in the theory of mergers—a simplified test to prove illegality—was elaborated upon in \textit{United States v. Phila-}


\textsuperscript{68} 370 U.S. 294 (1962) (J. Stewart and J. Fortas took no part in the case; J. Douglas concurred); Asch, \textit{supra} note 58, at 56.

\textsuperscript{69} Brown Shoe Co. v. United States, 370 U.S. 294, 346.

\textsuperscript{70} \textit{Id.} at 344.

\textsuperscript{71} \textit{Id.} at 315-19.
The merger in question would have created a bank with 30% of the relevant market. As a consequence of this merger, moreover, four banks would have controlled 78% of the same relevant market. Under these circumstances, illegality would be presumed without "elaborate proof of market structure, market behavior or probable anti-competitive effects." One observer concluded that, "with the Philadelphia Bank decision, the position of the volumes on oligopoly theory became secure on the shelves of antitrust lawyers and the general direction of the development of a legal policy aimed at controlling oligopoly power was established." In fact, the Court in the Philadelphia Bank case paid homage to the Congressional design to prevent undue concentration and concluded that mergers resulting in an undue percentage share of the relevant market inherently would tend to lessen competition substantially. Illegality was to be presumed "in the absence of evidence clearly showing that the merger is not likely to have such anti-competitive effects."

The Court's new position on oligopoly was again manifested in a case involving the purchase, by Alcoa, of the Rome Cable Corporation. Alcoa, a producer of 27.8% of aluminum conductor output, purchased the Rome Cable Corporation which produced only 1.3%. Rome, which was but one of four remaining independents in the field, was characterized by the Court as an aggressive competitor displaying special aptitudes and skills. Indeed, it was the prototype of the small independents that Congress aimed to preserve by section 7. According to the Court, the tendency towards oligopoly in this particular industry with its likelihood of parallel policies might well be thwarted by the presence of small but significant competitors.

A case which caused a good deal of consternation was United States v. Von's Grocery Company in which the third largest grocery chain in Los Angeles sought to merge with the sixth largest. The statistics in the ten-year period prior to the merger showed that the twenty largest grocery firms had increased their market share from 44% to 57% and that the share of the market held by the 12 largest firms progressed from 38.8% to 48.8%. What seemed to bother the critics of the majority opinion was the Court's emphasis on absolute numbers rather than upon market share. However, despite these shortcomings, there would seem to be ample justification for the view that "where concentration is gaining momentum in a market [the Supreme Court] must be alert to carry

73. Id. at 363.
74. Brodley, supra note 32, at 303.
77. Id. at 280.
79. Id. at 290.
out Congress' intent to protect competition against ever-increasing concentration through mergers.\footnote{80}

Despite the differences among scholars over the interpretation of antitrust laws as applied to horizontal and vertical mergers, there exists some consensus in these areas as to mergers which can and should be prohibited under section 7 of the Clayton Act. This area of agreement, however, does not extend to conglomerate mergers. Possibly it might be appropriate to define these different kinds of mergers since the conglomerates are sometimes referred to as those mergers which are neither horizontal nor vertical. A horizontal merger is one that takes place between two companies engaged in the same or similar lines of endeavor for the same geographical market. A vertical merger is the combining of two companies with a buyer-seller relationship. The remaining mergers which are conglomerate have been categorized by the Federal Trade Commission as market extension mergers, production extension mergers, and others. Market extension mergers simply refer to the acquisition of a firm doing the same kind of business in other area markets. Production extension is the merger of two firms whose products are sufficiently related so as to allow for the common use of certain management or marketing services. The "other" category is sometimes designated as a pure conglomerate and connotes mergers of totally unrelated products, services or facilities.\footnote{81}

Conglomerate mergers, at least for market extension or production extension purposes, would no doubt take place for many of the same reasons as horizontal and vertical acquisitions. Some of the reasons for conglomerate mergers briefly summarized are the desire to purchase a firm in a profitable industry, tax benefits, empire building, greater managerial challenge, the pooling of financial resources, and the fostering of reciprocal buying.\footnote{82} In terms of the present epidemic of conglomerates, however, one would have to agree with those who view the primary motivation as financial rather than competitive. The reason for the popularity of merger brokering is strikingly explained in the following quotation:

The acquiring company is often seeking to create a reputation as an acquisition-minded "growth" company. The preliminary objective is to attract merger partners and to implant in the minds of the public an expectation of future growth sufficient to cause the stock of the company to sell at a high multiple of earnings—perhaps 20 or 30 times earnings, as opposed to a more conservative 10 times earnings—and the company will thus be enabled to acquire other firms in stock-for-stock transactions at a favorable exchange ratio. If all goes well, the process is self-generating; a company selling at 30 times earnings exchanges a third of its

\footnote{80. Id. at 277.}
\footnote{81. Hearings, supra note 5, at 515.}
\footnote{82. Rudolph, The Rationale Behind the Foreclosure Doctrine, 46 Neb. L. Rev. 605, 620-21 (1967).}
stock (plus some increment for incentive) for control of a company with equal earnings but whose stock sells at only 10 times earnings. The earnings of the acquiring company are doubled, but the amount of stock outstanding is increased by only a third. Thus, earnings per share rise approximately fifty percent in a single quarter. This large apparent increase in earnings encourages investors to seek the company’s stock, which is driven to a new high and can again be used to make another acquisition at a favorable exchange ratio. This process does not by its own logic require that the acquired company be integrated into the acquiring one. Many of the new conglomerates function virtually as holding companies, with the central corporate headquarters doing little but reviewing quarterly reports from subsidiaries, arranging financing, and planning new acquisitions. Nor is it necessary that the companies be engaged in related fields. At a recent seminar on mergers, this author heard the acquisitions director of a successful conglomerate state, ‘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.”

There are those who feel it is an absurdity to attack a true conglomerate merger “in order to maintain competition, because it has no effect on any market structure.” Another somewhat less skeptical observer, although doubting that recent conglomerate mergers raise any particular anti-trust problems, nevertheless expresses the view that a day of reckoning may come when the conglomerates will seek to integrate operations. “This probability is the reason why anti-trust is not really rendered irrelevant by the fact that a company buys other firms without regard to competitive consequences and initially operates them as autonomous subsidiaries.”

Professor John M. Blair has accused a number of eminent legal authorities of attempting deliberately to exclude conglomerates from the sanctions of section 7. According to him, this attitude may be explained by their refusal (1) to utilize the tendency-toward-monopoly test, (2) to take into account the theories of anticipatory reaction with its emphasis on psychological response, (3) to believe that the Court may not take into consideration the economies of scale in applying the law, and last, and most important from the view of a political scientist, (4) to understand that Congress was concerned not only with “the maintenance of competition, but also the preservation of certain social and political

83. Davidow, Conglomerate Concentrations and Section Seven: The Limitations of the Anti-Merger Act, 68 COLUM. L. REV. 1231, 1238 (1968) [hereinafter cited as Davidow].
85. Davidow, supra note 83, at 1239.
values to which Congress, rightly or wrongly, attached great importance. 86

An examination of the Supreme Court's decisions regarding conglomerate mergers will provide a basis for determining the judicial response to the four major issues enunciated by Professor Blair. This analysis for purposes of convenience will classify a number of basic cases involving conglomerates into two major categories: A) potential competition, and B) the leverage power of the conglomerate.

A. Potential Competition

In United States v. El Paso Natural Gas Company, 87 no actual competition existed between El Paso, the sole out-of-state natural gas supplier to the California market, and Pacific Northwest, which had failed to penetrate the California market. Yet, Pacific Northwest, despite its unsuccessful efforts to enter the California market, had been able to force El Paso to lower its prices. In responding to the contention that there was no actual competition between the two companies, the Court noted:

We would have to wear blinders not to see that the mere efforts of Pacific Northwest to get into the California market, though unsuccessful, had a powerful influence on El Paso's business attitudes within the state. We repeat that one purpose of § 7 was "to arrest the trend toward concentration, the tendency to monopoly, before the consumer's alternatives disappeared through merger..." 88

In United States v. Penn-Olin Chemical Company, 89 Pennsalt and Olin Mathieson, while maintaining their separate identities, created a new entity Penn-Olin Chemical Company, for the purpose of producing and selling sodium chlorate in the southeastern part of the United States. Each company had evidenced interest in independently entering the chlorate field before the formation of the joint venture. The Supreme Court held that the district court had erred in failing to consider the probabilities that either of the parents "might have remained at the edge of the market, continually threatening to enter." 90 In an oligopolistic market, "the existence of an aggressive, well equipped and well financed corporation engaged in the same or related lines of commerce... would be a substantial incentive to competition which cannot be underestimated." 91 The district court was reminded that the mandate of Congress was to be considered

88. Id. at 659.
89. 378 U.S. 158 (1964); the case, upon being remanded to the District Court, was dismissed on the grounds that it was not probable that either of the parent companies would have entered the field independently. United States v. Penn-Olin Chem. Co., 246 F. Supp. 917 (D. Del. 1965), aff'd, 399 U.S. 308 (1967) (4:4 decision).
91. Id. at 174.
"in terms of the probability of a lessening of substantial competition, not in terms of tangible present restraints."\(^{92}\)

Continental Can Company v. United States\(^{93}\) dealt with the issue of inter product competition, and concerned a merger between a producer of metal cans and a producer of glass containers. Neither of the producers had ever been competitors and each was generally producing containers for exclusively different purposes. Critics may hold that the market definition in this case was somewhat exaggerated. However, the new school of economics has consistently taught that substitute products are a form of new competition. If this be the case, then one would have to concur with the Court's view that it would make little sense to expect the glass and metal entities within the Continental empire to compete for the same end use. The Court once again affirmed that a merger in which the acquiring firm is a "dominant firm in a line of commerce in which market power is already concentrated among a few firms" is inherently suspect, and elaborate proof of market structure and behavior and probable anti-competitive effects could be dispensed with.\(^{94}\)

B. Leverage Power

United States v. Procter & Gamble Company\(^{95}\) involved a product extension merger in which Procter, with 54% of the detergent market, absorbed Clorox with nearly half of the household bleach market. Procter is one of the nation's 50 largest firms. The question was whether a conglomerate had a peculiar kind of power resulting from the diversity of its own product area which would rub off on its new conquests. The highlights of the Court's decision are as follows: first, the Court reiterated that all mergers are within the reach of section 7 and that all must be tested by the same standard whether they be horizontal, vertical, conglomerate, or other;\(^{96}\) second, possible economies cannot be used as a defense for mergers which lessen competition;\(^{97}\) third, there was every reason to assume that smaller firms would be dissuaded from aggressively competing;\(^{98}\) fourth, the entrance of Procter would make oligopoly more rigid, and Procter probably would become the price leader;\(^{99}\) fifth, the advertising discounts available to Procter constituted a major competitive weapon in the marketing of bleach and would have a tendency to raise the barriers to new entries;\(^{100}\) and, sixth, that the merger eliminated Procter as a potential competitor.\(^{101}\)

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92. Id. at 177.
94. Id. at 458, 464.
95. 386 U.S. 568 (1967).
96. Id. at 577.
97. Id. at 580.
98. Id. at 578.
99. Id.
100. Id. at 579.
101. Id. at 580-81.
Another significant case involving a similar kind of a merger was Federal Trade Commission v. Consolidated Foods.\textsuperscript{102} Consolidated, which owned food processing plants together with a network of wholesale and retail stores, acquired Gentry, Inc., a manufacturer principally of dehydrated onion and garlic. The Federal Trade Commission held that the acquisition gave Consolidated "the advantage of a mixed threat and lure of reciprocal buying in its competition for business," and the "power to foreclose competition from a substantial share of the markets for dehydrated onion and garlic."\textsuperscript{103}

These latter decisions (Continental and Procter), dealing with the more readily recognized conglomerates, taken in conjunction with the precedent set by earlier cases involving potential competition, have erased a good deal of the mystery from the law pertaining to conglomerates. In both Procter & Gamble and General Foods, it was the "power" of the conglomerates to intimidate, to discourage, and to dissuade that the Court frowned upon. Power was evil in some instances because of the psychological effect it might have upon existing or new entries and, in others, because of the strengthening of oligopoly, and, in still others, because of advantages that resulted from certain of the economies of scale.

Some economists are concerned with the differences between "real" economies of scale and those economies that are the products of leverage emerging purely from the economic power of the conglomerate. The political scientist hardly reflects this bias. Congress disowned all power which substantially lessened competition or threatened substantially to lessen potential competition or to create a tendency toward monopoly.

Moreover, the mere existence of this . . . 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 goodwill of the possessor.\textsuperscript{104}

IV. THE 1960'S: THE BIRTH OF A NEW REVOLUTIONARY SPIRIT

As the 1890's were the heydays of the trust, so this decade is rapidly emerging as the golden age of the conglomerates. The Oil Trusts, the Sugar Trusts and the Tobacco Trusts are only memories, but Ling Temco Vought, Gulf & Western Industries and International Telephone and Telegraph are today amassing corporate empires with such verve and voraciousness that one suspects the age of the moguls is not past.\textsuperscript{105}

A comparison of the growth of conglomerate mergers between the periods 1951-54 and 1963-66 provides ample evidence to support the above

\textsuperscript{102} 380 U.S. 592 (1965).
\textsuperscript{103} Id. at 593.
\textsuperscript{105} Davidow, supra note 83, at 1231.
quotation. In terms of the large mergers, those involving acquisitions of $10 million or more in assets, conglomerates accounted for 51% in the 1951-54 period and 71% in the more recent period. Numerically, conglomerate mergers have increased more than 600%. Dollarwise, the earlier mergers involved some $1.3 billion as compared to over $10 billion in 1963-66.

More recent data showed that by 1967, conglomerates had increased to 83% of the total of large mergers and 80% of the assets of such mergers. Conglomerate growth, which today has reached significant proportions, may have been stimulated until recently by a deliberate policy of the government to concentrate primarily upon horizontal and vertical mergers. The conglomerate, at this moment, is a kind of last frontier for the growth of industrial empires. Thus, a strong case may be made for reversing Professor Turner's relative hierarchy of rules for mergers by pressing hardest on conglomerate mergers.

Senator Phillip A. Hart would concur with this conclusion. He is convinced that it is power not efficiency that is the driving force of the giant corporation. He believes the reasons for such mergers to be more understandable to the accountant or the investment banker than to the lawyer or the engineer. Computers, innovative industrial technologies, and low capital requirement products signify to the Senator the beginning of a new industrial revolution—a revolution which is more advantageous to the small rather than to the giant corporation. He is convinced that small and medium size firms have demonstrated far greater industrial ingenuity and inventiveness than the large industrial complex.

There is in the nature of democratic authority a kind of evolution from unilateral or monolithic to polycentric. The existence of multiple avenues of access—legislative, judicial, executive, and administrative—in the same sphere of government, allows the citizen to indulge in a kind of comparative policy shopping. The desire to disperse authority was expressed by the founding fathers in their advocacy of the principle of separation of powers. In a similar manner, the pluralistic nature of our society provides alternative routes to policy making through different spheres of public government—national, state, local, and county, and through varying countervailing forces of private government such as industry, labor, and agriculture. It is the multiplicity of these access areas that is of vital importance to the open society.

President Lyndon B. Johnson’s Task Force on Antitrust Policy, chaired by Phil C. Neal, believed that the preservation of a large number and variety of decision-making units in the economy is important to ensure innovation, experimentation, and continuous adaptation to new

conditions. Moreover, antitrust policy is viewed as reflecting a direct preference for private decision-making, which consequently minimizes the need for government intervention in the operation of business.

This observer would concur with the views of the many scholars who are skeptical of the role of government as a regulator. Certainly the history of government regulations, as exemplified by agencies such as the Interstate Commerce Commission and state public utility commissions, all too frequently reveal that the agency's viability is dependent on its subservience to the very clientele it is intended to regulate. Critics of antitrust are far too eager to recommend that resort be to regulation rather than promotion of the competitive market structure. The Johnson Task Force, however, showed no such compunctions and recommended that the antitrust laws be amended to provide for a specific legislative remedy directed to bring about a reduction in oligopolies or highly concentrated industries through divestiture, if necessary. Absent such direct action, there was little likelihood of any significant decline in concentration. The Task Force believed that it was not advocating any new policy but was simply reinforcing the existing public philosophy toward concentration. The recommended legislation would aim where feasible to reduce a four-firm concentration ratio of aggregate market share to below 50% and the market share of the individual firm to below 12%.

In keeping with this spirit, the Task Force would also provide specific prohibitions of certain kinds of conglomerate mergers. Merger guidelines established in 1967 by the Justice Department's Antitrust Division, while quite restrictive of horizontal and vertical mergers, were far more tolerant of conglomerate mergers. The Task Force proposal, on the other hand, would prevent conglomerate mergers between very large firms and other large firms that were already leading firms in significant concentrated markets in the national economy. The prohibition of such mergers would no longer rely on "conjectural judgments" and would lessen reliance on "extended and contrived interpretations of section 7." Instead, the emphasis of these proposals would be to improve the competitive structure of American Industry.

The Nixon Task Force on Productivity and Competition, chaired by George J. Stigler,109 did not share the philosophy of the Johnson group and seriously doubted that the Antitrust Division of the Department of Justice "should embark upon an active program of challenging conglomerate enterprises on the basis of nebulous fears of size and economic power." Instead, the Nixon Task Force proposed that a conference be called so as "to identify the problems, if any, created by the large conglomerate enterprise." A similar position was taken by the Task Force concerning proposals to deconcentrate highly concentrated industries by dissolving their leading firms. Here, too, the rationale was the inadequacy of present

knowledge as to the effects of oligopoly on competition. Antitrust apparently was to be viewed only from the vantage point of "good economic sense", and the Task Force cautioned against the temptation to utilize the antitrust laws to combat social problems not related to the competitive functioning of the markets.

The Stigler report perpetuated the myth that antitrust laws are concerned only with the economics of the marketplace and opts for a preferred or Platonic position for the economist-advisor, free from the distractions plaguing social and political analysts. Unfortunately for the Nixon Task Force, the economic, political, and social objectives of the antitrust laws are part and parcel of the same fundamental philosophy of a democratic society based upon diffusion of power. Attorney General John M. Mitchell recognized this interrelatedness when he stated, "[w]e have constructed a complex economic structure which successfully reflects adherence to the political and social principles of our free society."110

Because of the dangers posed by the economic concentration of conglomerate mergers to the vitality of a free economy and the aspirations for a free society, Mr. Nixon's Attorney General, contrary to the recommendations of the Nixon Task Force, promised to strengthen the antimerger guidelines. He warned that the Department of Justice might oppose any merger among the top 200 manufacturing firms or firms of comparable size in other industries.

Mr. Mitchell's fear that superconcentration leads to a control of the nation's manufacturing and financing resources in the hands of fewer and fewer persons is hardly a novel and quixotic concept but is nevertheless reflective of a new revolutionary spirit which is sweeping the land. Students, blacks, and others among the alienated and disillusioned are clamoring for the right to participate in decisions affecting their basic existence. Perhaps, the emphasis upon what has come to be known as participatory democracy is an outgrowth of the affluent society with its rising expectations. The depression psychology of the Thirties led to disenchantment with the uncertainties of the market place. Security replaced competition in the affections of business, agriculture, and labor. The obsession with security fathered the myth of the inevitability of concentration, and the belief persisted that one could not exist without the other. The revolution of the Seventies challenges this concept, and, more strongly than ever, demands the dispersal of power, particularly in the private sphere. The philosophy of the antitrust "is founded on a theory of hostility to the concentration in private hands of power so great that only a government of the people should have it."111 To this observer, the modern conglomerate qualifies as that kind of private power concentrate, and the Supreme Court, in applying section 7 to conglomerates, has interpreted the Act "in the light of its legislative history and of the particular evils at which


the legislation was aimed.\textsuperscript{112} Further recognition of the need for more intensive control of conglomerates has recently taken several forms: a strengthening of the relevant tax laws\textsuperscript{113} and more restrictive requirements by a number of administrative agencies.\textsuperscript{114} However, the times may require a still further expansion of the antitrust law, to strengthen the position of the courts in the field of antitrust, and to reaffirm the nation's basic belief in the diffusion of power in both the political and economic spheres.

\textsuperscript{112} Apex Hosiery Co. v. Leader, 310 U.S. 489 (1940).

\textsuperscript{113} The Tax Reform Act of 1969 (PL 91-172) limits the amount of interest a corporation is allowed to deduct on "corporate acquisition indebtedness" and also provides that certain indebtedness when received in the year of sale be included in the year of sale payment. Section 7 Clayton Act Comm. Rep., ABA Antitrust Section, Conglomerate Corporations and Acquisitions: Recent Developments, 8-9 (Supp. April, 1970).

\textsuperscript{114} A merger Notification Program announced in 1969 by the Federal Trade Commission would apply to merger transactions involving firms with assets of $10 million or more, and combined assets of $250 million or more (405 A-1, April 15, 1969). The Commission also adopted a new procedure for handling pre-merger clearance (411 A-2, May 27, 1969). In the summer of 1969, the Security and Exchange Commission announced its requirement for segmented profitability disclosure by diversified enterprises. (Rel. 33-4988). The Commission also promulgated Rule 10b-13 which in a take-over situation prevents the offerer from purchasing the stock of the target company except pursuant to the terms of the offer. (Rel. No. 8712). \textit{Id.} at 10-12.