THE SEMINAL CASES OF THE 1960S

THE COMMON LAW APPROACH TO ANTITRUST LAW. The federal antitrust statutes are written in broad, sweeping terms which by themselves provide little indication of the line between lawful and unlawful conduct. The Sherman, Clayton and Federal Trade Commission Acts, in contrast to most modern statutes regulating microeconomic behavior, were not intended to provide an instant cure for the perceived competitive problems of the day. The framers of the antitrust statutes recognized that the diversity and rapidly changing nature of business conduct, if not the inadequacy of contemporary economic theory to determine the root causes of anticompetitive behavior as well as the reactions of the trusts to attempts to regulate them, made a definitive statutory cure impossible.

Instead, Congress consciously adopted a more fluid, evolutionary approach to competition policy. Rather than specifying a rigid, detailed regulatory scheme, the draftsmen used sparse, broadly phrased language to describe the key substantive concepts in the new antitrust law—"contract, combination or conspiracy," "restraint of trade," "monopolize, or attempt to monopolize," and "unfair competition"—language that is almost unique among congressional enactments in its constitution-like quality. These concepts, drawn from the common law, were employed to empower federal courts to apply immediately a large existing body of competition law to regulate business conduct. But the Sherman Act was written not to codify the common law once and for all as it existed in 1890. Rather, it was designed to enable the courts over time through the common law process to refine the law and its application to particular courses of conduct. As Senator John Sherman candidly stated during the course of the debate:

> I admit it is difficult to define in legal language the precise line between lawful and unlawful combinations. This must be left to the courts to determine in each particular case. All that we, as lawmakers, can do is to declare general principles, and we can be assured that the courts will apply them so as to carry

> out the meaning of the law, as the courts of England and the United States have done for centuries.[1]

Similarly, Senator Hoar, the floor manager for the Sherman bill after it was reported from the Judiciary Committee, observed:

> Now, the Judiciary Committee has carefully and as thoroughly as it could agreed upon what we believe will be a very efficient measure, under which one long forward step will be taken in suppressing this evil. We have affirmed [in the Judiciary Committee redraft] the old doctrine of the common law in regard to all interstate and international commercial transactions, and have clothed the United States courts with authority to enforce that doctrine by injunction. We have put in also a grave penalty.[2]

Senator George F. Edmunds, chairman of the Judiciary Committee, expressed a second, even more pragmatic, reason to empower the courts to develop the precise boundaries between lawful and unlawful conduct rather than look in the future to refining legislation from Congress:

> The trouble about this business [of drafting an antitrust law] is as I have seen a good many times before when we were trying to strike at great evils in a broad way and leave the details and difficulties that might arise afterwards to be repaired by legislation, as we do about all such things, that Congress has failed to make a law because the very person against whom it was intended to operate in their mischievous performances got up, as they say on the prairies, a counter-fire and added to the fuel and stimulated men to carry the so far that it could not be executed at all.
>
> That was the aspect of this thing when this subject was sent to the Committee on the Judiciary. We all felt, and the committee, I think unanimously, including my friend from Mississippi [Senator James Z. George], thought that if we were really earnest in wishing to strike at these evils broadly, in the first instance, as a new line of legislation, we would frame a bill that should be clearly within our constitutional power, that we should make its definition out of terms that were well known to the law already, and would leave it to the courts in the first instance to say how far it or its definitions as applicable to each particular case as it might arise.[3]

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1. 21 Cong. Rec. 2460 (Mar. 21, 1890). *See* 21 Cong. Rec. 2456 (Mar. 21, 1890) (the Sherman bill "does not announce a new principle of law, but applies old and well-recognized principles of the common law to the complicated jurisdiction of our State and Federal Government") (remarks of Sen. Sherman); *id.* at 2461 ("This bill declares a rule of public policy in accordance with the rule of the common law.") (remarks of Sen. Sherman).

2. 21 Cong. Rec. 3146 (Apr. 8, 1890).

3. *Id*. at 3148. See George Edmunds, The Interstate Trust and Commerce Act of 1890, 194 North American Rev. 801, 814 (Dec. 1911) ("After most careful and earnest consideration . . . [the Senate Judiciary Committee thought that] it was quite impracticable to include by specific description all the acts which should come within the meaning and purposes of the words 'trade' and 'commerce' or 'trust,' or the words 'restraint' or 'monopolize' . . . and that there were truly matters for judicial consideration.").

As we shall see, the courts have had a difficult enough time in attempting to fashion a sensible competition law within the broad foundations laid by the Sherman Act. Senator Edmunds was certainly correct that the task could not realistically be left in the hands of Congress, and wisely Congress has, for the most part, left the antitrust laws to the courts to discern and has not attempted to fine tune the law through legislation.

As Congress intended, when statutes are vague and uninforming as they are in antitrust, it falls upon the courts to resolve the ambiguities and provide the guidance necessary for the rule of law to operate. As Justice (later Chief Justice) Harlan F. Stone once observed:

> The prohibitions of the Sherman Act were not stated in terms of precision or of crystal clarity and the Act itself does not define them. In consequence of the vagueness of the language, perhaps not uncalculated, the courts have been left to give content to the statute, and in the performance of that function it is appropriate that courts interpret its words in the light of its legislative history and of the particular evils at which the legislation was aimed.[4]

Since the turn of the century, an enormous body of precedent has been created by the federal courts and the Federal Trade Commission to fill the interstices of statutory antitrust law and provide guidance on the probable legal status of a wide variety of business activities and arrangements, including mergers and acquisitions. Although literally hundreds of merger antitrust cases have been decided by the courts, four Supreme Court cases—United States v. E.I. du Pont de Nemours & Co.,[5] Brown Shoe Co. v. United States,[6] United States v. Philadelphia National Bank,[7] and United States v. General Dynamics Corp.[8]—form the core of contemporary merger antitrust law.

Briefly, *du Pont*, a 1957 decision applying the original 1914 version of Clayton Act § 7 but very much influenced by the concerns of the 1950 Congress in passing the Celler-Kefauver Act discussed above in the excerpt from *Brown Shoe*, established the broad applicability of the act to all types of horizontal, vertical and conglomerate mergers and acquisitions (including those in which only a minority interest has been obtained), confirmed the construction of Section 7 to reach anticompetitive transactions in their incipiency without waiting for an anticompetitive effect to mature, determined that the proper time at which to assess the effects of a transaction is at the time of suit and not at the time of the acquisition, and vividly illustrated the impotency of the doctrine of laches in Section 7 cases by ordering divestiture of stock acquired forty years prior to the decision. *Du Pont* created many of the foundations of modern merger antitrust law. *Brown Shoe,* the

4. Apex Hosiery Co. v. Leader, 310 U.S. 469, 489 (1940).
5. 353 U.S. 586 (1957).
6. 370 U.S. 294 (1962).
7. 374 U.S. 321 (1963).
8. 415 U.S. 486 (1974).

1962 case that was the Court's first decision to apply the new substantive standard under the 1950 amendments and that remains the single most important merger antitrust case from a developmental perspective, reaffirmed the requirement that an unlawful merger must entail a reasonable probability of some substantial anticompetitive effect in a market (as opposed to a mere lessening of rivalry between previously competing firms) and emphasized the critical nature of market definition in merger antitrust analysis. In 1963, *Philadelphia National Bank* created a presumption that entitles the plaintiff, at least in horizontal mergers, to establish the requisite anticompetitive effect for a Section 7 prima facie violation from statistical evidence of the market shares of the merging parties and changes in the level of concentration the merger would entail in the markets in which the parties operate. Over ten years later, in 1974, *General Dynamics* reasserted the rebuttable nature of the *Philadelphia National Bank* presumption, which in the intervening years had rapidly become conclusive, and invited deeper economic analysis of mergers and acquisitions in assessing their legality.[9] The *PNB* presumption, as clarified by *General Dynamics*, remains today the de facto exclusive way of establishing a prima facie Section 7 violation in horizontal mergers.

UNITED STATES V. E.I. DU PONT DE NEMOURS & CO. (1957). [10] *DuPont* was the first merger case to reach the Supreme Court after the passage of the Celler-Kefauver Act in 1950.[11] Although the Court agreed that the challenged acquisition of stock, which occurred through various purchases between 1917 and 1919, was governed by the original 1914 version of Section 7, the decision very reflects the concerns of the 1950 Congress. In light of its preeminence on the questions of incipiency, laches, post-acquisition evidence, and the foreclosure of competitors as an anticompetitive harm, not to mention the case's inherently fascinating character, the du Pont/GM decision merits close attention. The decision also serves as the point of departure for the judicial activism in antitrust cases of the Warren Court generally and of William Joseph Brennan, Jr., a newly appointed associate justice and author of the four-to-two majority opinion, in particular. This activism is quite vivid given the sorry state of the Supreme Court's explication of the facts underlying its decision, a

9. Two other cases could have been added to this list. *Falstaff Brewing* and *Marine Bancorporation*, decided in 1973 and 1974 respectively, legitimized the application of merger antitrust law to conglomerate transactions by recognizing that, at least in some circumstances, the elimination of potential competition can serve as the predicate for the anticompetitive harm required for a Section 7 violation. *See* United States v. Falstaff Brewing Corp., 410 U.S. 526 (1973); United States v. Marine Bancorporation, Inc., 418 U.S. 602 (1974). We will return to them in Unit 5, when we examine nonhorizontal mergers. *Baker Hughes*, a unanimous D.C. Circuit decision authored by then-Judge Clarence Thomas and including then-Judge Ruth Bader Ginsburg on the panel, is the seminal opinion on the allocation of the burden of proof in merger antitrust cases. *See* United States v. Baker Hughes, Inc., 908 F.2d 981 (D.C. Cir. 1990).

10. 353 U.S. 586 (1957).

11. Pub. L. No. 81-899, 64 Stat. 1125 (1950).

fact made all the more poignant by the district court's view that the case really was about a Sherman Act conspiracy and not the legality of a 30-year old minority stock acquisition under the Clayton Act.[12]

The case broadly challenged Du Pont's involvement in the management and operation of the General Motors Company. General Motors was organized by William C. "Billy" Durant in 1908, the same year that Henry Ford produced the first Model T. Durant, the controlling investor in the Buick Motor Company—the largest automobile manufacturer of the day—created GM as a holding company under which to consolidate as much as the nascent car industry as he could gather. In addition to Buick, Durant soon brought under the GM aegis Cadillac, Oakland (renamed Pontiac in 1926), Oldsmobile, six other automobile companies, three truck firms, and ten parts and accessory manufacturers. Notwithstanding the size and success of his company, Durant's acquisition spree left him with little working capital and Durant was caught short by the slight business recession in the summer of 1910. When car sales dropped off, Durant found himself unable to pay for workers or supplies. Durant was forced to borrow $14 million to meet GM's working capital requirements from a banking syndicate led by Lee, Higginson and Company of Boston. As a condition of the loan, Durrant deposited his GM shares into a five-year voting trust and turned control of the company over to the bankers. Unwilling to be part of an organization he could not run, Durant left GM. He joined with former Buick racer Louis Chevrolet to found the Chevrolet Motor Company to produce a new low-priced car. Durant, however, by no means had lost interest in General Motors, and through Chevrolet began buying substantial amounts of GM stock and trust certificates.

Du Pont's involvement in GM began in February 1914. Pierre S. du Pont, by then the controlling force in the family's hundred-year old firm, E.I. du Pont de Nemours

12. Unfortunately, neither the trial court nor Supreme Court is especially lucid on the circumstances surrounding the Du Pont stock purchases and involvement in General Motors. A more complete story can be found in ALFRED D. CHANDLER, JR. & STEPHEN SALSBURY, PIERRE D. DUPONT AND THE MAKING OF THE MODERN CORPORATION 433-604 (1971); ALFRED D. CHANDLER, JR., STRATEGY AND STRUCTURE: CHAPTERS IN THE HISTORY OF INDUSTRIAL ENTERPRISE 115-22 (1962); ARTHUR POUND, THE TURNING WHEEL: THE STORY OF GENERAL MOTORS THROUGH TWENTY-FIVE YEARS, 1908-1933 ch. 10 (1934); LAWRENCE H. SELTZER, A FINANCIAL HISTORY OF THE AMERICAN AUTOMOBILE INDUSTRY 145-72 (1928); and STAFF OF SUBCOMM. ON ANTITRUST AND MONOPOLIES OF THE S. COMM. ON THE JUDICIARY, 84TH CONG., BIGNESS AND CONCENTRATION OF ECONOMIC POWER—A CASE STUDY OF GENERAL MOTORS CORPORATION (Comm. Print 1956). The description in the text draws considerably from these sources.

Powder Company (reorganized in 1915 into E.I. du Pont de Nemours & Co.[13]), purchased 2000 shares of the six-year old automobile company as a personal investment at the urging of John J. Raskob, Pierre's closest business associate and the Du Pont Company treasurer. Raskob, who also had bought 500 shares stock for his own account, argued that the GM stock was substantially undervalued at the then-current market price of $70 per share, a prediction that proved more than prescient. By December 1915, the price of GM stock had hit $558 per share, driven both by the strong demand for cars as well as by Durant's efforts to accumulate additional GM stock. By that time, Pierre had increased his GM holdings to over 2300 shares, and his GM investment now comprised over half of the value of his outside investment portfolio.

Given these holdings, Pierre must have found attractive the invitation of Lewis G. Kaufman, president of the commercial bank the Du Pont Company used in New York City and one of Durant's principal backers, to join the GM board. When Pierre arrived at the September 1915 meeting, he was surprised to find that, contrary to Kaufman's representation, Durant did not have practical control of the company and did not have the power to unilaterally place Pierre on the Board. Indeed, the Durant and Lee, Higginson factions were deadlocked on the composition of the slate of new directors to guide GM after the Durant voting trust expired. After much debate, the two factions could agree on only twelve of the fifteen directors, six directors for each side. To break the deadlock, James J. Storrow, a senior partner of Lee, Higginson, offered a compromise—Pierre, one of the Durant-Kaufman nominees, would nominate three "neutral" candidates to fill the remaining director slots. Durant agreed, and Pierre named Raskob, J. Amory Haskell, a retired Du Pont vice president and board member, and Lammot Berlin, Pierre's cousin and brother-in-law. As part of the agreement, Pierre was to become chairman of the GM board. The slate was approved at the annual shareholders meeting in November, and for the next thirteen years Pierre served as GM's chairman.

Notwithstanding Lee, Higginson's efforts to impose some order on the sprawling GM empire, Pierre found the automobile company a loose confederation of assembly and parts facilities and distribution firms. This was just the opposite of the tightly run Du Pont Company, which Pierre had made into the first true modern corporation. Pierre was rebuffed, however, in his efforts to institute the same management and financial controls in GM as he had in Du Pont. Much to Pierre's surprise, Durant had continued through Chevrolet Motors to acquire GM stock after the September board meeting and in late December 1915 announced not only his claim to control of the company but also of his intent to merge GM with Chevrolet. Pierre and the three "neutral" directors in fact remained neutral in this second round of the Durant-Storrow battle (refusing, for example, Durant's invitation to purchase in Chevrolet), but by April 1916 it was clear that Durant, even given Pierre's neutrality, controlled over 50 percent of GM's stock. The Boston bankers resigned from the GM board,

13. The 1915 reorganization completed the restructuring of the company as a result of the government's successful Section 1 attack against the Powder Trust. *See* United States v. E.I. du Pont de Nemours, Eq. 280 (D. Del. June 13, 1912) (opinion and final decree).

and Charles W. Nash, who as president ran GM for the bankers, and Henry Leland, the founder and continuing head of the Cadillac subsidiary, retired rather than work under Durant. The bankers and Nash formed a new venture, the Nash Motor Company, while Leland began the Lincoln Motor Company. Durant took over the GM presidency, and, while he urged Pierre and his associates to remain on the GM board and to become members of the General Motors Finance Committee, Durant clearly intended that the board be no more than an advisory body that he had to have to meet legal requirements. The founder of General Motors did not ask for nor would he tolerate any help in running the company. He did, however, freely discuss GM's future plans with Pierre.

Durant began a major expansion of GM, financed largely by the company's high earnings, and by the end of December 1917 investment in plant and equipment had almost doubled. While Pierre had been disturbed by the size and manner of the expansion, he was too involved in the Du Pont Company's wartime efforts and family litigation over the control of the company to interfere with Durant's plans. Instead, Pierre had appointed Raskob, the Du Pont Company treasurer and always the more enthusiastic of the two about the automobile company, as his deputy and spokesman at GM. All too soon both the Chevrolet/GM merger and the continuing plant expansion had been jeopardized by the entry of the United States into the war, which had precipitated an enormous drop in the price of automobile stocks as stock buyers worried about possible steel rationing, excess profits taxes, and price controls. By mid-September, 1916, GM stock had dropped to $86 and was continuing to fall. Apparently Durant (and perhaps Raskob as well) had been purchasing GM stock on margin, and with the drop in the stock price Durant's personal position had become critical. After several failed attempts to find money from other sources, Durant and Raskob finally approached the Du Pont Company itself. Du Pont had vast wartime surpluses, and, as Raskob well knew, $50 million of which remained unallocated to the company's planned postwar diversification. Moreover, the Secretary of War had just rejected the contract Du Pont had signed with the Army Ordnance Department to build the largest smokeless powder plant in the world, leaving Du Pont at a loss for a major project to devote its attention and talents. Raskob proposed that Du Pont invest $25 million in the stock of GM and Chevrolet, $3 million to be purchased from Durant and the rest on the open market, a move explicitly designed to support the stock's market price. Pierre believed that the growth of the automobile industry in the United States after the war appeared as certain as anything could in business, and agreed to support the proposal provided that Chevrolet be merged into GM (eliminating Durant's independence), that the same types of administrative controls he had earlier recommended be instituted, and that the GM Finance and Executive Committees be patterned after those at Du Pont. Pierre and Durant agreed that Du Pont would run GM's finances through control of the Finance Committee, while Durant, working through the Executive Committee, would have full authority for GM's operations.

The proposal came somewhat as a shock to the Du Pont board at its December 1917 meeting. Only three weeks before, the board had approved the largest contract ever negotiated with the United States government, and now it was being asked to approve one of the largest investments ever made by an industrial company in a firm operating in a wholly unrelated market. The board was initially split, with questions over whether the smokeless powder plant contract was really dead and even if so whether GM was the right place for so large an investment. Raskob argued that the funds were available even if the smokeless powder plant was revived and that GM provided an unsurpassed opportunity for the investment of surplus funds, yielding 40 percent if historical earnings continued. In addition, Raskob pressed upon the board that the purchase would give the Du Pont Company, together with Durant and Pierre, joint control of GM and Chevrolet, that Du Pont would be responsible for the financial operations through its control of the GM Finance Committee, and finally—to the skeptics and those working on the diversification program—that "our interest in General Motors will undoubtedly secure for us the entire Fabrikoid, Pyralin, paint and varnish business of these companies, which is a substantial factor."[14] Pierre took a slightly different tack with the board. He argued that GM could become even more profitable with the benefit of Du Pont's experience in management and financial controls, and that the Du Pont Engineering Department and other staff units, threatened with excess capacity now that the war plants were complete, could be of service to the GM as the automobile industry continued its enormous growth. Pierre also stressed that the dividend cash flow from GM would be especially valuable in the near term as Du Pont began new ventures such as in paints, dyes, and artificial silk that likely would not be profitable for some time. The Pierre/Raskob arguments prevailed, and the Du Pont board approved the GM investment. A new intermediate holding company, General Industries, Inc. (soon to become Du Pont American Industries, Inc.) was formed, and by March 1918 it had purchased 99,875 shares of General Motors and 133,690 shares of Chevrolet for $25,183,759. The 133,600 shares of Chevrolet stock converted into the equivalent of 152,788 General Motors shares, so that the purchases gave Du Pont 23.83 percent of the GM's outstanding stock.[15] To keep its percentage interest roughly constant in the wake of new stock issues by General Motors and Chevrolet, Du Pont purchased an additional 1,966,665 GM shares and 25,515 Chevrolet shares for $21,238,159 by the end of 1918. Its total investment in 1918 of $42,539,012 in 206,454 shares of GM and 159,115 shares of Chevrolet translated into the equivalent of 26.35 percent of the outstanding stock of the General Motors.[16]

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14. Memorandum dated December 19, 1917, to the Du Pont Company Finance Committee from the Treasurer [Raskob] re General Motors-Chevrolet Motor Stock Investment 11, Gov't Ex. ___, *quoted in* United States v. E.I. du Pont de Nemours & Co., 126 F. Supp. 235, 245 (N.D. Ill. 1954), *rev'd*, 353 U.S. 586, 602 (1957).

15. History of the Du Pont Company's Investment in the General Motors Corporation dated August 17, 1921, Gov't Ex. 166.

16. *Id*.

Cumulative Du Pont Investments in GM and Chevrolet 1917-1921

Year	General Motors		Chevrolet		Total GM Equivalent		
	Shares	Dollars	Shares	Dollars	Shares	Dollars	%
1917	5,600		40,200		515,406	$3,628,160	6.7
1918	2,064,540	$25,228,940	159,115	$17,310,072	3,882,906	$42,539,012	26.35
1919	2,385,040	$31,448,181	159,115	$1,310,072	4,408,983	$48,758,253	28.74
1920	1,124,312	$13,249,434	253,490	$32,674,984	4,926,662	$45,924,418	23.96
1921	6,882,108	$71,289,540	33,294	$4,291,719	7,362,540	$75,581,259	35.80

Holdings each year as of December 31 except for 1921, which is as August 17, 1921. GM shares are shown in their 1920 equivalents, reflecting a one-for-ten stock split on May 5, 1920.

In 1920, as the general postwar recession continued to shake the economy, GM was once again strapped for working capital, while Durant found himself overextended on his personal stock speculations to the tune of $27 million of indebtedness. The Du Pont Company gained control of additional GM shares through the purchase of newly issued stock as well as through a complicated bailout of Durant organized with the help of J.P. Morgan. As a result, in mid-1921 Du Pont controlled 7,362,540 shares, or about 35 percent, of the GM stock outstanding, valued at roughly $75 million. As a condition of his bailout, Durant resigned from active management. Pierre reluctantly accepted the GM presidency, which he held until 1923 when he relinquished the post to Alfred P. Sloan, Jr. Pierre himself retired as chairman of the GM board in 1928, after which time he had little or nothing to do with the active management of the company. Also in 1923, Du Pont began selling some of its GM stock, and by 1938 had returned to a 23 percent stake, where it remained for the next several decades.

So much for the Du Pont Company's stock investment in General Motors. Now what of the use of this investment for purposes the Supreme Court found 40 years later were anticompetitive? On June 30, 1949, the Department of Justice filed a complaint in the Northern District of Illinois charging the Du Pont Company, General Motors Corporation, United States Rubber Company, three du Pont family investment companies, and three individual members of the du Pont family (including Pierre) with conspiracy to restrain trade and monopolization of various products produced by the three defendant manufacturers in violation of the Sherman Act, and further charging the Du Pont Company with acquiring a controlling interest in General Motors through its purchases in 1917 through 1919 in violation of Clayton Act § 7. The district court clearly thought that the case was about a restraint of trade conspiracy, and devoted almost all of its 100-page opinion to whether the defendants in fact used their stock interests to control the management of the defendant manufacturers. While the court found that the du Pont family did control the Du Pont Company, it did not find any agreement, understanding or conspiracy that the family members would continue to hold the vote, keep it within their family, or use their shareholdings to create protected markets or otherwise restrain or monopolize trade. As to General Motors, the court found that the du Pont defendants never had voting control over the company, although the defendants' stock was voted as a block and always in the majority, and at least since 1923 were always in the minority on the board. The court also noted that, although a number of individual du Ponts and their associates served as highly placed officers and directors of GM, others, particularly Sloan, were equally influential in the company and ensured that GM remained independent. The court found no agreement that GM would purchase it all or any portion of its requirements from the Du Pont Company, and that the Du Pont defendants never intended to preclude GM from dealing with suppliers of its choice, never made any effort to so preclude GM, and did not in fact limit GM's freedom in purchasing from third parties. Although no doubt the du Pont defendants were keenly interested in obtaining orders for the Du Pont Company from General Motors, the court found that such trade could be secured only on a competitive basis. According to the district court, rather than seeking to use their stock holdings to benefit the Du Pont Company, and presumably harming GM, the du Pont defendants regarded their interest in General Motors (and in United States Rubber) as investments whose value should be protected and maximized.[17] Since there was no agreement among the defendants to restrain trade, there was no Section 1 violation. More specifically, since there was no agreement made in connection with the Du Pont investment to foreclose any trade with GM by third parties and since the du Pont interests did not obtain control of GM through their shareholdings, there could be no Section 7 violation. Accordingly, the district court dismissed the government's complaint.

The Supreme Court, on a direct appeal under the Expediting Act, disagreed on the Section 7 conclusion and did not address the Section 1 holding. To Justice Brennan, writing for a four-to-two majority, the central issue was whether "du Pont's commanding position as General Motor's supplier of automotive finishes and fabrics was achieved on competitive merit alone" or was the result of a "close intracompany relationship" due to Du Pont's acquisition of GM stock that insulated GM from third-party competition.[18] After concluding that automotive finishes and fabrics constituted the appropriate relevant market in which to analyze the acquisition, the Court observed that at and around the time that the complaint was filed General Motors accounted for roughly 40 percent of automobile sales in the United States and presumably at like percentage of automotive finishes and fabrics. The Court then noted that Du Pont supplied 67 percent of GM's requirements for finishes in 1946, and 68 percent in 1947, and that in fabrics it supplied 52 percent and 38.5 percent in the same two years respectively. Justice Brennan concluded, as a result, that Du Pont supplied a substantial part of the automotive finishes and fabrics market; it only remained to determine whether its success stemmed from the competitive merit of its products and prices or from anticompetitive foreclosure of GM's requirements to third-party manufacturers resulting from Du Pont's stock interests.

17. *Id*. at 242-43.

18. 353 U.S. at 588-89. Justices Burton and Frankfurter dissented, while Justices Clark, Harlan and Whittaker did not participate in the case.

Justice Brennan begin this stage of the analysis by noting that Du Pont's sales to GM were relatively insignificant until shortly after its first purchase of a sizeable block of stock in 1917. The Court cited Raskob's original recommendation to the Du Pont board that one of the advantages of the purchase would be that: "Our interest in the General Motors Company will undoubtedly secure for us the entire Fabrikoid, Pyralin, paint and varnish business of those companies, which is a substantial factor." Not surprisingly, the predicted Du Pont/GM vertical business relationships that formed the basis for the Court's finding of unlawful vertical foreclosure soon began to materialize. All told, the Court pointed only to three bits of evidence relating Du Pont's "control" of GM to the foreclosure of competitors. First, the Court gave great weight to a 1921 query by Pierre to Lammot du Pont, Pierre's brother, first vice president of the Du Pont Company and chairman of its Executive Committee, "whether General Motors was taking its entire requirements of du Pont products from du Pont," and Lammot's reply that four of GM's eight operating divisions bought from Du Pont all of their requirements of paints and varnishes, five their requirements of Fabrikoid (an artificial leather), four their requirements of rubber cloth, and seven their requirements of Pyralin (celluloid), and that the prospects for the future for supplying all of the requirements of all of the divisions were improving.[19] Second, by 1926, of all the GM operations only the Fisher Body Company, then 60 percent owned by GM but with a voting trust giving the Fisher brothers a great deal of independence, was obtaining any substantial portion of its requirements from Du Pont's competitors; by 1947, when Fisher "resistance had collapsed," Fisher purchases of its requirements from Du Pont were roughly similar to those of other GM divisions.[20] Third, once a GM division began to purchase its requirements from Du Pont, it continued to do so over time through the lawsuit; the Court speculated that purchases were made from competitors largely because GM's demands outstripped Du Pont's production.[21] The Court concluded that Du Pont "purposely employed its stock to pry open the General Motors market" and that its position as the primary supplier of GM fabrics and finishes "was not gained solely on competitive merit."[22] Justice Brennan poetically concluded:

> The fire that was kindled in 1917 continues to smolder. It burned briskly to forge the ties that bind the GM market to duPont, and if it has quieted down, it remains hot, and, from past performance, is likely at any time to blaze and make the fusion complete.[23]

Having found a violation of Section 7, the lower court was instructed to fashion appropriate relief. The district court's plan to "sterilize" the Du Pont block interest by passing the voting rights in the GM stock pro rata to Du Pont shareholders (except

19. 353 U.S. at 604.
20. *Id*. at 604-05.
21. *Id*. at 605.
22. *Id*. at 604, 605.
23. *Id*. at 607.

for Du Pont entities) was rejected by the Supreme Court in a later decision,[24] and ultimately Du Pont was required to divest its GM shares.[25]

The *Du Pont/GM* decision raises a number of troubling questions: Was Justice Brennan justified in concluding that from 1917 forward Du Pont's sales to GM were the proximate result of Du Pont's 1917 stock purchase, in order to provide the (probable) causal link between the original stock purchase and the foreclosure of the automobile fabrics and finishes market necessary to yield a Section 7 violation? What is the significance of the facts that, at the time of the original purchase, automobile fabrics and finishes standing alone could not have constituted a relevant antitrust market, much less one subject to anticompetitive foreclosure, and that to the extent such a market emerged it did so only years later as the automobile industry grew in size and advanced in technological sophistication? Indeed, should the Court have considered the facts that, particularly in the early years after the stock purchase, Du Pont was far and away the leader in research and development in automobile fabrics and finishes--and as such responsible for the very uniqueness that enabled the Court to conclude in 1957 that these products formed a relevant product market for antitrust purposes—and that Du Pont's incentives to innovate in this area stemmed largely from its ownership interest in GM? What are the limits of use of post-acquisition evidence to prove a Section 7 violation? Although the Court's conclusion turned on the question of control, should the analysis take into account Du Pont's acquisition of a minority interest in GM as opposed to 100 percent of the company? And just what was the theory of threatened anticompetitive harm in the case anyway?

BROWN SHOE CO. V. UNITED STATES (1962).[26] *Brown Shoe* was the first merger antitrust case the Supreme Court decided under the Celler-Kefauver Act. In November 1955, the Department of Justice filed suit seeking to block the merger of the Brown Shoe Company (of "Buster Brown" fame) and the G.R. Kinney Company, two major shoe companies, on the grounds that the combination would violate the recently amended Section 7 of the Clayton Act in the production, distribution and retail sale of shoes. The district court denied the government's motion for a blocking preliminary injunction pendent lite. Instead, the court entered a preliminary injunction in the form of a hold separate order which permitted the transaction to close provided that, after the closing and until the suit was resolved, the business of Kinney would be held in a subsidiary corporation with directors and officers independent from Brown, all of Kinney's assets and subsequent net earnings would be kept in this subsidiary

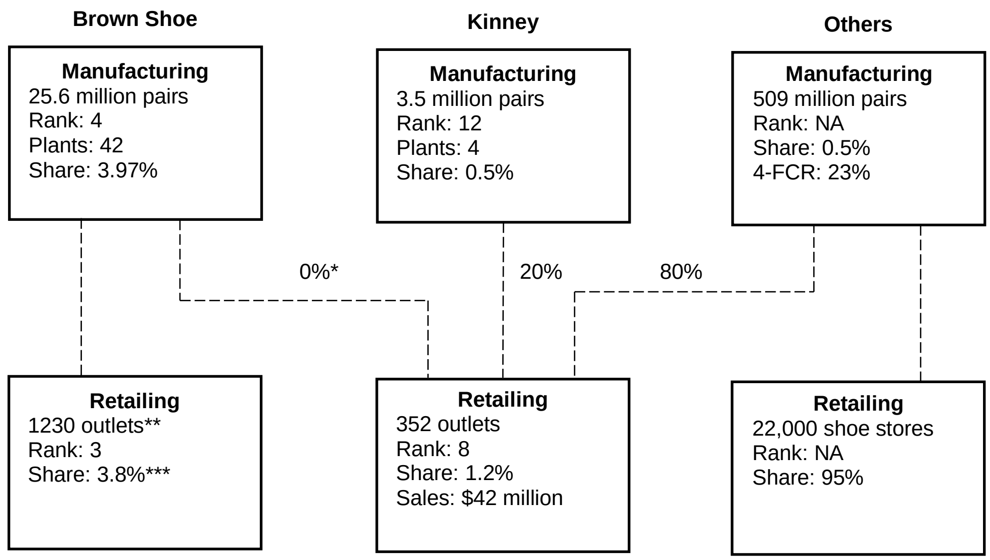
24. 366 U.S. 316 (1961), rev'g 177 F. Supp. 1 (N.D. Ill. 1959).

25. 1962 Trade Cas. (CCH) ¶ 70,245 (N.D. Ill. 1962).

26. 370 U.S. 294 (1962), *aff'g* 179 F. Supp. 721 (E.D. Mo. 1959). *See generally* John L. Peterman, *The Brown Shoe Case*, 18 J. L. & ECON. 81 (1975).

and not intermingled with those of Brown, and no Kinney factories or retail outlets would be closed by reason of competition with Brown.[27] Subject to these conditions, the transaction closed on May 1, 1956.[28]

The Brown Shoe/Kinney Merger
(operations prior to closing)



* 7.9% after merger
** Includes owned stores (470), independently owned franchised stores (570), and independently owned stores under the “Wohl plan” featuring Brown-manufactured shoes (190)
*** Excludes franchised stores

At the time of the acquisition, domestic shoe production remained fragmented among a large number of manufacturers, but producers were rapidly consolidating as well as acquiring independent retail outlets. Brown was a leading participant in the consolidation of the industry. Through a series of acquisitions, Brown had become the fourth largest shoe manufacturer in the United States, although it produced less than four percent of the footwear manufactured domestically. Seven of its 42 plants had been acquired since 1948. Although Brown had experimented in operating a few

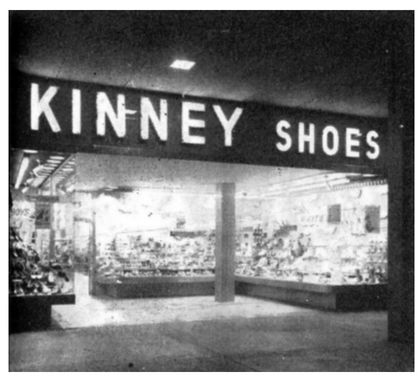
27. The hold separate order is reported at 1956 Trade Cas. (CCH) ¶ 68,244, at 71,117 (E.D. Mo. 1956). *See also* United States v. Brown Shoe Co., 179 F. Supp. 721, 724 n.4 (E.D. Mo. 1959); *Shoe Merger Barred*, N.Y. TIMES, Jan. 17, 1956, at 48 (reporting on conditions of hold separate order).

28. *See*

retail outlets, it had disposed of its retail operations by 1945. Beginning in 1951, however, Brown began to reintegrate into retailing, primarily through the acquisition of several previously independent retailers, most notably the Wohl Shoe Company (250 stores) and the Regal Shoe Corporation (110 stores). By 1955, Brown had become the third largest seller of shoes at retail with 1250 outlets (845 of which it had acquired) and sales of over $159 million. Retail outlets acquired by Brown quickly turned to the manufacturer for an increasing share of their shoe requirements, regardless of their buying relationship with Brown prior to their acquisition.

Kinney, on the other hand, was primarily a retailer. It was the nation's largest family-style shoe store chain and the eight largest retailer of shoes generally. At the time of its acquisition, Kinney operated over 350 stores in more than 270 cities. Its $42 million in sales accounted for about 1.2 percent of the total shoe sales in the country by dollar volume. Kinney was also the twelfth largest shoe manufacturer in the United States. Its four manufacturing plants accounted for approximately 0.5 percent of national shoe production. Kinney retail stores obtained about 20 percent of their shoes from Kinney's own manufacturing facilities and the rest from third-party manufacturers.

With the acquisition of Kinney, Brown moved from the fourth largest to the third largest shoe manufacturer, with approximately five percent of total domestic shoe production. Moreover, the acquisition gave Brown more retail outlets than any other manufacturer and moved it from third to second in net sales of shoes at retail nationwide. While prior to the merger Kinney bought no shoes from Brown, by 1957 Brown had become Kinney's largest outside supplier, accounting for 7.9 percent of all Kinney's requirements, and was continuing to grow in importance as a supplier. For its part, Kinney supplied a rapidly increasing percentage of the shoes it produced to Brown retail outlets, while diminishing its sales to independent retailers.



The Brown/Kinney transaction was representative of what was happening generally in the shoe industry as well as many other segments of the economy in the post-war economy. New distribution methods, particularly through standardized chain stores, were rapidly gaining a real comparative advantage in the marketplace against the more traditional, more fragmented independent distribution arrangements. At the same time, improvements in manufacturing technologies and techniques gave rise to additional economies of scale. Finally, firms were becoming more adept at managing multi-plant enterprises and realizing the efficiencies possible through them. Given these developments, many industries once populated with many small independent manufacturing firms and retail outlets began to experience a consolidation both at the manufacturing level and at the retail level, as well as a vertical integration between manufacturing and retailing. In the shoe industry, for example, many small independent manufacturers were being acquired by larger firms or simply going out of business. Between 1950 and 1956, 159 plants exited the market, reducing the number of operating plants from 1207 to 1048. Seven companies operating 25 plants were acquired by one of the ten largest shoe manufacturers. Manufacturers were also acquiring retailers. In 1945, for example, the International Shoe Company had no retail outlets; by 1956 it had acquired 130 retail stores. The General Shoe Company had only 80 retail outlets in 1945 but had 526 by 1956. In the same time period, Shoe Corporation of America increased its retail holdings from 301 to 842 stores, Melville Shoe Company grew from 536 to 947 stores, and Endicott-Johnson from 488 to 540 stores. Brown, as we have seen, had disposed of its retail stores by 1945, but was back in the retailing business with 845 acquired outlets by 1956. Altogether, between 1950 and 1956, nine independent shoe store chains, operating 1114 retail stores, had become subsidiaries of a large manufacturing firm. By 1956, the six largest shoe manufacturers operated 3997, or just over 18 percent, of the nation's 22,000 shoe stores. Not surprisingly, once manufacturers acquire retail outlets, they tend to increase the sale of their own products to these outlets at the expense of competing smaller, independent manufacturers, just as Brown did after it acquired Wohl and Kinney.

Trial began on August 4, 1958, over two years after the acquisition was consummated. Testimony ended on January 24, 1959, and the cause was taken under submission on August 1, 1959. The district court decided the case on November 20, 1959. After briefly reviewing the history of the Clayton Act and the 1950 amendments, the court held that the amended statute required it to address three issues: (1) the relevant line of commerce in which to assess the acquisition; (2) the relevant section of the country; and (3) the impact of the acquisition on competition.

The Justice Department argued at trial that the acquisition would tend substantially to lessen competition by eliminating actual and potential competition in two distinct markets: "the production of shoes for the national wholesale shoe market" and "in the sale of shoes at retail in the Nation."[29] In both of these alleged markets, the government argued, competitive harm would result "by foreclosing competition from 'a market represented by Kinney's retail outlets . . .' and by enhancing Brown's competitive advantage over other producers, distributors and sellers of shoes."[30] The Justice Department also alleged in the alternative that the relevant "line of commerce" affected by the Brown/Kinney merger could be "men's," "women's," and "children's" shoes considered individually and that the "section of the country" could be each separate city in which the parties to the transaction sold shoes at retail.

Brown responded that the relevant "lines of commerce" were delineated not only by the age and sex of the intended wearers but also by differences in grade of material, quality of workmanship, price and customer use of the shoes. Brown agreed that for the purpose of assessing the effect of the merger in shoe production the relevant geographic market was the country as a whole, but contended that with

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30 *Id*. at 297.

respect to retailing the market, depending on area in question, varied from the central business district of a large city to a standard metropolitan area for a smaller community.

The district court rejected the primary product market definition contentions of both parties, finding that men's, women's, and children's shoes separately—but not shoes as a whole—were the relevant lines of commerce in which to analyze the likely competitive effects of the merger in both manufacturing and retailing. The district court held a "line of commerce" means a relevant product market, that is, a group of products that has "peculiar characteristics and uses which make it distinguishable from all other products."[31] In particular, the court held that in assessing the dimensions of the relevant product market, the trier of fact should examine: (1) the practices of the industry; (2) the characteristics and uses of the product; (3) their interchangeability; (4) their price; (5) their quality; and (7) their style. Applied here, the court found that there is interchangeability in the production processes of shoes, but in fact manufacturers separate into different facilities the manufacture of men's, women's and children's shoes. There is also interchangeability in use between shoes of many different styles and prices, but that no interchangeability between men's and women's shoes and little interchangeability between adult's and children's shoes. Finally, the industry and the public recognize men's, women's and children's shoes as distinct classes of shoes. Accordingly, the court held that men's, women's and children's shoes, considered separately, were the relevant lines of commerce in which to assess the competitive impact of the transaction.

The Justice Department and Brown both agreed, and the district court found, that the relevant section of the country of geographic market in which to assess the transaction's competitive effect in manufacturing was the United States. The parties disagreed, however, over the relevant geographic market in which to assess the impact on retailing. The court noted that the relevant geographic market is defined to be the "area of effective competition."[32] Interestingly, the court cautioned that this area of effective competition cannot "be determined solely from testimony of economists," but must also take into account the testimony of businessmen as to the where and whose competition they meet.[33] Kinney and Brown both apparently only operated shoe stores in cities with 10,000 or more in population. Moreover, the evidence showed that Brown franchise dealers in downtown metropolitan areas were competing with Brown franchise dealers in the outlying commercial areas as well as with other retailers. The same was true of Kinney retail outlets. The court held that the relevant sections of the country in which to examine the transaction's effect in retailing were the 141 cities with 10,000 or more in population and the immediate and contiguous surrounding areas (without regard to political boundaries) in which both a Kinney store and a Brown store (operated, franchised, or plan) were located.

[31] 179 F. Supp. at 729, *quoting* United States v. E.I. du Pont de Nemours, 353 U.S. 586, 593 (1957).

[32] 179 F. Supp. at 733 (*quoting* Standard Oil Co. of California v. United States, 337 U.S. 293, 299 n.5 (1949) ("*Standards Stations*")).

[33] 179 F. Supp. at 733.

Both the government and the defendants introduced considerable evidence pertinent to the dimensions of the market in St. Louis, where the court was sitting, and the opinion suggests that the judge was influenced considerably by this evidence and extrapolated the St. Louis experience to other cities in which Brown and Kinney operated.

Turning to the impact of the merger on competition, the district court held that, as a matter of law, a merger or acquisition may substantially lessen competition within the meaning of Section 7 if the transaction: (1) substantially increases concentration in the relevant market; (2) eliminates a substantial factor in competition; (3) eliminates a substantial source of supplies; or (4) results in vertical relationships between buyers and sellers that deprive the rivals of one of the merging parties of "the fair opportunity to compete."[34] The court also noted that congressional concern with the trend toward concentration in American industry, the plight of small businesses, and the inability of the Sherman Act to reach small acquisitions that nonetheless added to the power of an already large firm motivated passage of the Celler-Kefauver Amendments in 1950. The court stressed that a transaction's ultimate legality would turn not so much on the share percentages of the combining firms in isolation but rather on "what these percentages mean in examination under the light of the facts of the case and economic realities involved," especially those about which Congress was concerned.[35]

Using these standards, the district court summarily rejected the government's contention that combining the manufacturing facilities of Brown and Kinney would by itself substantially lessen competition in the manufacture of shoes for sale into the national wholesale market. The court noted that the transaction could only slightly affect commerce in the nationwide manufacturing market by increasing Brown's production from 5 percent to 5.5 percent of domestic production. The court also may be been influenced by the evidence, noted earlier in the opinion, that although manufacturing concentration increased with the disappearance of 159 plants between 1950 and 1956, there remained 1048 plants in operation at the time of the acquisition. Moreover, in the same period, only seven significant companies (operating a total of 25 plants) were acquired by the ten largest shoe manufacturers, causing only a small increase in concentration as a result of acquisition. Finally, as of 1956, only 212 plants, or about 20 percent of the total, were owned by the top ten producers.[36]

The district court did find, however, that when the vertical aspects of the combination were taken into account, the transaction likely would foreclose competing manufacturers from that part of the retail market occupied by Kinney's retail outlets. This resulted in anticompetitive effects in two distinct types of markets:

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[34] 179 F. Supp. at 736. This four-element test is taken directly from United States v. Bethlehem Steel, 168 F. Supp. 576, 603 (D.D.C. 1958).

[35] 179 F. Supp. at 737.

36. The Supreme Court noted that, after the Kinney acquisition, the top four shoe manufacturers—International, Endicott-Johnson, Brown (including Kinney), and General Shoe—produced approximately 24 percent of the nation's shoes. 370 U.S. at 300.

> *National wholesaling market:* The court noted that the record revealed a definite trend of manufacturers acquiring retail outlets, and that after an acquisition manufacturers tended to increase the sale of their own products to these outlets at the expense of competing smaller, independent manufacturers. The court found Brown to be a moving factor in these trends. On these findings, the court concluded that the Kinney acquisition would lessen competition between Brown and other manufacturers in the manufacture and wholesale of men's, women's and children's shoes throughout the United States by decreasing the competitors' share of sales to the acquired Kinney outlets. Moreover, to the extent that the larger size of the combined companies provided Brown with commercial advantages in buying materials, selling, advertising and the like (*i.e.*, the integrative efficiencies of the transaction), the combined company would be able to further increase its sales relative to third-party retailers. This, in turn, would increase Brown's power to control prices and tend to create a monopoly in manufacture and distribution.
>
> *Local retailing markets*: In addition, the court also found that the acquisition would lessen retail competition in men's, women's, and children's shoes in cities of 10,000 or more in population (and the contiguous surrounding area) in which both a Kinney and a Brown Shoe store are located, due to Kinney's advantages in buying and pricing that would result from being part of the Brown organization. The impact here would be felt by competing local retailers, which would confront a more efficient firm. It also would be felt small independent manufacturers which would suffer a decrease in the outlets for their products not only from the displacement of their products from Kinney stores but also from the decline of independent retailers relative to Kinney. The result, the court concluded, would be a substanitally lessening of competition and a tendency to monopoly in these local retailing markets.

In both the national wholesaling market and the local retailing markets, the district court obviously was concerned that the industry trend, in which Brown had already significantly contributed in the eyes of the court, was toward the elimination of small manufacturers and independent retailers. The Kinney acquisition, which would bring under Brown's dominion the nation's largest family style shoe store chain, was just one more step in this process. The court entered judgment for the government, ordered Brown to dispose of its Kinney stock, made permanent the preliminary hold separate injunction pending divestiture, and enjoined both Brown and Kinney in the future from acquiring stock of the other.

Brown appealed directly to the Supreme Court under the Expediting Act.[37] Although the Celler-Kefauver Act had amended Section 7 of the Clayton Act over ten years before, this was the first case before the Court where the government had alleged a violation of the revised statute. In an opinion by Chief Justice Earl Warren joined by at least four associate justices, the Court affirmed the lower court's judgment that Brown's acquisition of Kinney violated the amended Section 7. Justice Tom C. Clark concurred in at least the result (his opinion is not clear as to how

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37. For contemporary newspaper reports, see, for example, *High Court Hears Brown Shoe Case*, N.Y. TIMES, Dec. 7, 1961, at 63.

much, if at all, he agreed with the majority's reasoning), while Justice John Marshall Harlan II, grandson of the Justice Harlan of *Northern Securities* fame, dissented as to the Court's jurisdiction but concurred in the result, although not the majority opinion, on the merits.[38]

Chief Justice Warren began the majority's analysis with a lengthy examination of the legislative history of the 1950 amendments. To the Court, the extensive congressional attention devoted to merger antitrust amendments, coupled with the general language finally adopted by Congress, made it necessary to examine the legislative history to ensure that whatever result was reached in the case was consistent with congressional intent.[39] Although we already have examined this history in detail in Chapter 4, it is important in understanding the place of Brown in the evolution of merger antitrust law to be clear about precisely what the Court said about this history. Specifically, the Court found that the legislative history of the Celler-Kefauver Act revealed that Congress amended Section 7 to achieve the following eight enumerated objectives:

1. Plug the "asset loophole" and include asset acquisitions as well as stock acquisitions within the coverage of Section 7 of the Clayton Act.[40]
2. Clarify that Section 7 reached vertical and conglomerate mergers and acquisitions as well as horizontal transactions.
3. Stem the "rising tide of concentration" by arresting possibly anticompetitive transactions in their incipiency, before their anticompetitive effects could mature.
4. Ensure that anticompetitive threats not prohibited as actual restraints of trade by Section 1 of the Sherman Act could be reached.
5. Confirm that Section 7 addresses only anticompetitive effects in an economically significantly markets and that the statute protects competition, not individual competitors.
6. Leave unspecified the tests for determining the product and geographic dimensions of the relevant market within which the competitive effect of the merger was to be assessed and for what it means to "substantially" lessen competition.
7. Assure that the courts will use a "functional" approach to merger antitrust analysis and assess the likely effects of a transaction in context of the industries in which they occur, including:

38. Justice Felix Frankfurter, who was in the process of retiring (to be replaced by Arthur J. Goldberg), and Justice Byron R. White, who had just been appointed to the Court (replacing Charles Evans Whittaker), did not participate in the decision.

39. 370 U.S. at 312 (citing United States v. E.I. du Pont de Nemours & Co., 353 U.S. 586, 59192 (1957); Schwegmann Bros. v. Calvert Distillers Corp., 341 U.S. 384, 390-95 (1951); FTC v. Morton Salt Co., 334 U.S. 37, 43-46, 49 (1948); Corn Products Refining Co. v. FTC, 324 U.S. 726, 734-37 (1945)).

40. 370 U.S. at 316.

a. Whether the consolidation was to take place in an industry that was fragmented rather than concentrated.
b. Whether the industry had experienced a recent trend toward domination by a few leaders or had remained fairly consistent in its distribution of market shares among the participating companies.
c. Whether there was easy access by suppliers in the sale of inputs and easy access by buyers in the sale of outputs, or had the industry witnessed the foreclosure of business.
d. Whether the industry had witnessed the ready entry of new competition or the erection of barriers to prospective entrants.

8. Emphasize that, notwithstanding the concern with the rising tide of concentration, Congress used the words "may be substantially to lessen competition" to indicate that Section 7 addressed "probabilities, not certainties."[41] At the same time, the Court stressed, Section 7 prohibited only "clear-cut menaces to competition," not "ephemeral possibilities."[42] A merger or acquisition violated Section 7 if, but only if, it entailed a "probable anticompetitive effect" in a relevant market.

Interestingly, particularly in light of future developments, in a little noticed footnote accompanying the above litany the Court observed:

> [S]tatistics reflecting the shares of the market controlled by the industry leaders and the parties to the merger are, of course, the primary index of market power; but only a further examination of the particular market—its structure, history and probable future—can provide the appropriate setting for judging the probable anticompetitive effect of the merger.[43]

While all of the above eight factors ultimately would play an important role in the judicial development of merger antitrust law, the Court's caution about relying too much on market share data was quickly forgotten. But that takes us ahead of our story.

The Court made another observation centrally important to Clayton Act jurisprudence: the test of illegality under the Clayton Act is "less stringent" than that used in applying the Sherman Act. The Court noted that its Columbia Steel decision was interpreted by some in Congress to say that the Sherman Act was inadequate to prohibit mergers or acquisitions that would substantially lessen competition in some section of the country but that had not yet risen to the level of those restraints of trade

41. 370 U.S. at 323.

42. *Id*.

43. *Id*. at 322 n.38 (citing Pillsbury Mills, Inc., 50 F.T.C. 555 (1953); United States v. Bethlehem Steel Corp., 168 F. Supp. 576 (S.D.N.Y. 1958); United States v. Jerrold Electronics Corp., 187 F. Supp. 545 (E.D. Pa. 1960), *aff'd per curiam*, 365 U.S. 567 (1961); REPORT OF THE U.S. ATT'Y GEN. NAT. COMM. TO STUDY THE ANTITRUST LAWS 126 (1955)).

or monopoly prohibited by the Sherman Act.[44] The Court noted that both the House Judiciary Committee's 1949 report and the Senate Judiciary Committee's 1950 report agreed that the Clayton Act should impose a stricter standard on business conduct than the Sherman Act.[45]

Immediately following its general discussion of the Cellar-Kefauver Act's legislative history, the Court turned to consider the vertical aspects of the Brown/Kinney merger. Chief Justice Warren began by identifying the foreclosure of competitors as the principal competitive vice of vertical mergers à la du Pont. Warren's concern was that the tying of a customer to a supplier prevented the competitors of either from competing on a level playing field for business with the affiliated company and thereby acted as a "clog on competition."[46] Warren also noted that such foreclosure "deprives[s] . . . rivals of a fair opportunity to compete."[47] This last observation is somewhat at odds with the Court's view stated in its discussion of the legislative history that the Clayton Act is designed to protect competition, not competitors, unless the idea is that competition is affected when all (or at least some significant fraction) rivals are disadvantaged in their ability to deal with the integrated firm. Perhaps this is the reason that Warren did not find vertical mergers per se unlawful, but rather held that the Clayton Act required further analysis to determine whether the effect of the transaction "'may be substantially to lessen competition or tend to create a monopoly' 'in any line of commerce in any section of the country.'"[48] The Court could have made a similar observation about horizontal combinations, which necessarily eliminate competition between the merging rivals but do not necessarily threaten a substantial lessening of competition in the marketplace.

With these comments, Warren reaffirmed the *du Pont* observation that merger antitrust analysis bifurcates into a determination of the product and geographic boundaries of the relevant "line of commerce" and "section of the country" as well as an assessment of the competitive effect of the transaction within this market. Taken together, the line of commerce and section of the country in question is called a "relevant market" (there may be more than one in any transaction), one of the key terms of merger antitrust jurisprudence. Determination of the relevant market, therefore, is a necessary predicate to a Section 7 violation both because the statute speaks in these terms and, perhaps more fundamentally, because the "substantiality" of any anticompetitive threat—the dike preventing Section 7 from outlawing all vertical and horizontal mergers—can be assessed only in terms of the market affected.

44. **Error! Main Document Only.**370 U.S. at 318 n. 33 (citing 96 Cong. Rec. 16502 (Dec. 13, 1950) (remarks of Sen. Kefauver); H.R. REP. NO. 81-1191, at 10-11 (Aug. 4, 1949)).

45. **Error! Main Document Only.**370 U.S. at 318 n. 33 (citing H.R. REP. NO. 1191, 81st Cong., 1st Sess. 7-8 (Aug. 4, 1949); S. REP. NO. 81-1775, at 4-5 (June 2, 1950)).

46. 370 U.S. at 324 (quoting Standard Oil Co. of California v. United States, 337 U.S. 293, 314 (1949)).

47. 370 U.S. at 324 (quoting H.R. Rep. No. 81-1191, at 8 (. 4, 1949)).

48. **Error! Main Document Only.**370 U.S. at 324 (quoting Clayton Act § 7).

The *Brown Shoe* Court held that the "outer boundaries" of a product market are determined by the "reasonable interchangeability of use" and the "cross-elasticity of demand" between the products in question.[49] But these two concepts did not exhaustively identify all relevant "lines of commerce" for Section 7 purposes. Apparently building upon *duPont's* observation that "automotive finishes and fabrics have sufficient peculiar characteristics and uses to constitute them sufficiently different from all other finishes and fabrics to make them a 'line of commerce' within the meaning of the Clayton Act,"[50] the *Brown Shoe* Court formally recognized the existence of "submarkets," that is, relevant lines of commerce within the broader market defined by reasonable interchangeability of use and the cross-elasticity of demand. Submarkets, the Court said, could be determined

> by examining such practical indicia as industry or public recognition of the submarket as a separate economic entity, the product's peculiar characteristics and uses, unique production facilities, distinct customers, sensitivity to price changes, and specialized vendors.[51]

While the discussion in *Brown Shoe* initially addressed product submarkets, the *Brown Shoe* Court also applied the concept to "areas of the country" or geographic submarkets.[52] If a submarket was "economically significant," then it, like a "market" proper, was a "line of commerce" in a "section of the country" to which Section 7 applied. The Court held that, because Section 7 prohibits any merger or acquisition that may substantially lessen competition "in any line of commerce in any section of the country," the finding of the requisite anticompetitive effect in any relevant market or submarket is sufficient to make the combination unlawful, even if the transaction would be significantly procompetitive or have other socially redeeming virtues in other markets or submarkets.[53]

Significantly, although the *Brown Shoe* Court's discussion of submarkets clearly implied that not all of the enumerated indicia had to be present, the Court give no

49. **Error! Main Document Only.**370 U.S. at 325. The Court also observed in a footnote that "cross-elasticity of production"—presumably cross-elasticity of supply—could also be an important factor in defining product markets. *Id.* at 325 n. 42. The idea that supply-side substitution can be used to define product markets was never fully developed in the case law, and was ultimately rejected as a defining principle by the federal enforcement agencies beginning with the 1982 DOJ Merger Guidelines.

50. 370 U.S. at 325 (citing United States v. E.I. du Pont de Nemours & Co., 353 U.S. 586, 59395 (1957)). *Du Pont* did not employ the concept of "submarket," and the *Brown Shoe* Court did not say exactly why it was citing the case. The language from *du Pont* quoted in the text is the only suggestion I can find that links the case to the *Brown Shoe* submarket concept.

51. 370 U.S. at 325 (citing BETTY BOCK, MERGERS AND MARKETS: AN ECONOMIC ANALYSIS OF CASE LAW 25-35 (1960)).

52. 370 U.S. at 336 (citing Erie Sand & Gravel Co. v. FTC, 291 F.2d 279, 283 (3d Cir. 1961); United States v. Bethlehem Steel Corp., 168 F. Supp. 576, 595-603 (S.D.N.Y. 1958)).

53. 370 U.S. at 325 (citing United States v. E.I. du Pont de Nemours & Co., 353 U.S. 586, 592, 595 (1957) (decided under the original Section 7); A.G. Spalding & Bros. v. FTC, 301 F.2d 585, 603 (3d Cir. 1962); American Crystal Sugar Co. v. Cuban-American Sugar Co., 259 F.2d 524, 527 (2d Cir. 1958); United States v. Bethlehem Steel Corp., 168 F. Supp. 576, 603 (S.D.N.Y. 1958)).

indication of the relative importance of these factors or in any other way indicated a test or threshold to distinguish product groupings that constituted submarkets from those that did not. Nor did a test later emerge in the case law. The lack of a sharp principle to delineate submarkets was to leave the courts, the antitrust enforcement agencies and the public at sea in judging the legality of mergers and acquisitions as changes n the distribution of market share as the result of a consolidation later became the test of legality under Section 7. Probably no other concept has done as much damage to merger antitrust policy as that of submarkets.

Turning to the facts of the case, Warren found each of its submarket indicia satisfied separately for men's, women's, and children's shoes, but rejected Brown's further distinction of "price/quality" as "unrealistic" in identifying the boundaries of competition between differently priced products: "[T]he boundaries of the relevant market must be drawn with sufficient breadth to include the competing products of each of the merging companies and to recognize competition were, in fact, competition exists."[54] Glibly said, but to what extent exactly did shoes with different "price/quality" attributes actually "compete" with one another? Warren attempted to ridicule Brown's argument by suggesting that no one could question that men's shoes selling below $8.99 competed with men's shoes selling above $9.00 (remember, this was 1962), but the logic does not work. The proper question may not be whether men's shoes priced at $8.99 compete with men's shoes priced at $9.00, which is the thrust of the rhetoric, but rather whether men's shoes priced at $12.00 (or whatever the average price was for men's "medium-priced" shoes) compete with shoes priced at $7.00 (or whatever the average price was for men's "low-priced" shoes). The answer here is not obvious, yet the Court ignored the question. The Court's suggestion that companies that make and sell products that are functionally interchangeable, despite price differences that might make them practically distinct, can be in the same relevant product market, yet at the same recognizing that prices differences can create different relevant submarkets, opened the entire question of market definition to prosecutorial gerrymandering.

On the other hand, the majority found Brown's "age/sex" distinction as perhaps technically proper but unhelpful in analyzing the merger, since both Brown's and Kinney's respective market shares in narrower "youth's and boy's" shoes, "misses' and children's" shoes, and "infants' and babies'" shoes to mirror their shares in the broader line of all children's shoes. Since the further distinction made no difference to the result, the majority agreed with the district court that to subdivide further the lines of commerce on the basis of age and sex would be "impractical" and "unwarranted."[55] Certainly it must be correct that whenever alleged differences in market boundaries do not make a difference in the final result, the courts should not be required to devote significant time and energy to resolving the market definition issue.

54. 370 U.S. at 326.

55. *Id*. at 327.

As to the "section of the country," the Supreme Court also agreed with the parties and the lower court that the relevant geographic market with respect to manufacturing was the United States as a whole, and affirmed the lower court's finding that cities of a population exceeding 10,000 and their environs in which both Brown and Kinney retailed shoes through their own outlets constitute the relevant geographic markets for analyzing the horizontal retail aspects of the transaction.

Within these relevant markets, the Court agreed with the district court that the merger, when viewed as a vertical acquisition by a leading shoe manufacturer of a leading shoe retailer, may substantially lessen competition by foreclosing access to Kinney's retail outlets by Brown's manufacturing competitors in each of the three relevant national products markets. To reach this conclusion, Chief Justice Warren partitioned vertical mergers into three categories:

1. Vertical mergers that make "captive" a sufficiently large share of the foreclosed market—one approaching a monopoly—in which case the merger will be unlawful regardless of the surrounding circumstances, presumably including any efficiencies that the combination created.
2. Vertical mergers where the captive share is sufficiently small that the merger can be of no competitive consequence, and requires no further analysis to be sustained.
3. Vertical mergers that fall in between these two extremes and so require additional analysis of other pertinent "economic and historical factors."[56]

The *Brown Shoe* Court concluded that the Brown/Kinney merger, which at most foreclosed two percent of total shoe purchases (including captive sales) in any relevant market, fell in the third category.[57] Among the "most important" considerations to take into account were the nature and purpose of the challenged arrangement. These factors were typically the starting point in challenges under other sections of the Clayton Act, such as tying arrangements or exclusive dealing arrangements examined under Section 3 of the Clayton Act, and the *Brown Shoe* Court found that Congress intended that the same test of illegality apply under Section 7 as under other sections of the Clayton Act. In non-merger vertical restraint cases, the extent of competitor foreclosure was the primary determinant of illegality.

Analyzing the facts here, the *Brown Shoe* Court found that no consolidation between a shoe manufacturer and a shoe retailer could involve a larger potential competitor foreclosure. In addition, Brown's president had testified at trial that the company intended to distribute Brown products through Kinney retail outlets after the acquisition. Since Kinney did not distribute Brown products prior to the acquisition, the Court concluded that through the acquisition Kinney was "forced" to carry Brown shoes. This perceived "forcing" made the nature and effect of this

56. 370 U.S. at 329.

57. In the **Error! Main Document Only.**national product market, Kinney sold approximately 1 percent of men's shoes, 1.5 percent of women's shoes, and 2 percent of children's shoes. 370 U.S. at 303.

vertical merger analogous to a tying arrangement, which at the time of the decision merited the most stringent of antitrust scrutiny.

Moreover, the Court found that there was a trend toward concentration in the industry—more particularly the trend toward vertical integration and the decline of independent shoe retailers—and that Brown had contributed to this trend. This trend toward concentration and Brown's participation in it had two distinct implications for the Brown majority. First, the trend suggested that competitor foreclosure and oligopolistic behavior among the resulting larger, integrated firms would grow increasingly worse in the future, and that this was precisely the type of incipient anticompetitive behavior that Section 7 was designed to halt. But the effect of the Brown/Kinney merger on the economics of the marketplace did not end the analysis for the majority:

> [N]ot only must we consider the probable effects of the merger upon the economics 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. Congress was desirous of preventing the formation of further oligopolies with their attendant adverse effects upon local control of business and upon small business. Where an industry was composed of numerous independent units, Congress appeared anxious to preserve this structure.[58]

This suggests that even if competitor foreclosure or oligopolistic behavior was not a serious concern, the courts might still be justified in intervening to break up the acquisition—and presumably halt other acquisitions in the industry in the future—in order to preserve the existing atomistic structure of the shoe manufacturing industry.

Given the "forcing" of Kinney to carry Brown products and the significance of the resulting potential foreclosure of Brown's manufacturing competitors from Kinney outlets, and the trend toward vertical integration with its implications both for foreclosure and oligopolistic behavior in the future and for social structure of the shoe manufacturing industry, the Court affirmed the lower court's finding that the acquisition violated Section 7 with respect to distribution.

The Court next turned to the horizontal aspects of the transaction. Although the Justice Department did not appeal the district court's finding that the horizontal combination of Brown's and Kinney's manufacturing facilities did not threatened competition, Brown contested the lower court's conclusion that the acquisition may substantially lessen competition at the retail level. The Court introduced its analysis by observing:

> The effect on competition of such an arrangement [between competitors generally] depends, of course, upon its character and scope. thus, its validity in the face of the antitrust laws will depend upon such factors as: the relative size and number of the parties to the arrangement; whether it allocates shares of the market among the parties; whether it fixes prices at which the parties will sell their product; or whether it absorbs or insulates competitor. Where the arrangement effects a horizontal merger between companies occupying the same

58. 370 U.S. at 333 (footnotes omitted).

> product and geographic market, whatever competition previously may have existed in the market between the parties to the merger is eliminated. Section 7 of the Clayton Act , prior to its amendment, focused upon this aspect of horizontal combinations by proscribing acquisitions which might result in a lessening of competition between the acquiring and the acquired companies. The 1950 amendments made plain Congress' intent that the validity of such combinations was to be gauged on a broader scale: their effect on competition generally in an economically significant market.[59]

The Court reemphasized that market definition is a "necessary predicate" to the determination of a horizontal merger's legality under Section 7.[60] The Court also noted that, within a properly defined market, the "market share which companies may control by merging is one of the most important factors to be considered when determining the probable effects of the combination on effective competition in the relevant market."[61]

Since the government did not appeal the district court's finding that Brown's acquisition of Kinney did not threaten to substantial lessen competition at the manufacturing level, only the horizontal consolidation at the shoe retailing level was before the Court. Here, the Court found that the same product categories—men's, women's, and children's shoes—that constituted relevant product markets in the vertical analysis also were the proper relevant product markets for the horizontal analysis. As to the relevant geographic markets, the Court held that the trial record supported the finding that shoe stores on the outskirts of cities compete with shoe stores in central business districts, and affirmed the trial court's conclusion that the relevant geographic markets in which to analyze the merger's horizontal retail aspects were cities with a population exceeding 10,000 and their environs in which both Brown and Kinney had retail outlets.

The Court observed that, using premerger statistics, in women's shoes alone the combined share of the two companies at retail exceeded 20 percent in 32 cities. In children's shoes, the combined firm's retail share exceeded 20 percent in 31 cities and 40 percent in six cities. In some cities, the combined share in at least product market was over 57 percent. More generally, in 118 separate cities the combined share of Brown and Kinney exceeded 5 percent in at least one of the three relevant product lines, while in 47 cities the combined share exceeded 5 percent in all three lines.[62] In assessing the significance of these combined shares in local retail markets, the Court concluded that a combined share of as low as five percent was still sufficiently high to create a Section 7 concern for four reasons:

1. If a five-percent merger were allowed today, future mergers by Brown's competitors creating five-percent shares may have to be approved in the

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59. 370 U.S. at 334-35 (footnotes omitted).

60. *Id*. at 335.

61. *Id*. at 343 (citing United States v. E.I. du Pont de Nemours & Co., 353 U.S. 586, 595-96 (1957)). The Court also referenced Derek Bok, *Section 7 of the Clayton Act and the Merging of Law and Economics*, 74 HARV. L. REV. 279, 308-11 (1960).

62. 370 U.S. at 342-43.

future making it difficult to prevent the oligopolies Congress sought to avoid.

2. The significance of a five-percent share is magnified when that share is held by a large national chain, since national chains can "insulate" selected outlets from local competition as well as set and alter styles making it difficult for local independent stores to maintain competitive inventories.
3. The merger of a large national chain with a manufacturing firm may result in efficiencies that would permit the combined firm to underprice its non-integrated competitors, threatening the continued viability of small businesses about which Congress was most concerned.
4. The acquisition would contribute substantially to the already existing trend toward concentration at the retail level, directly contrary to "the mandate of Congress that tendencies toward concentration in industry are to be curbed in their incipiency, particularly when these tendencies are being accelerated through giant steps striding across hundreds of cities at a time."[63]

Since Brown and Kinney presented evidence of no mitigating considerations—the Court mentioned business failure, inadequate resources necessary to compete, or a need to combine in order to enable small companies to become more competitive in their markets as possible examples—the Court affirmed the lower court's judgment that the acquisition may tend to lessen competition substantially in the retail sale of men's, women's, and children's shoes in the "overwhelming majority" of the relevant local geographic markets.

Brown Shoe was pathbreaking in its emphasis on market definition and incipiency. At the same time, the decision left many essential questions unanswered: Exactly what is the test of market definition? What is the threat to competition that the antitrust laws prohibit? The market definition question remained unsettled for years, but the test for anticompetitive effect was answered, at least for making out a prima facie case, in the Court's next merger antitrust case.

NOTES

1. Brown Shoe was created to manufacture shoes in St. Louis in 1878 as Bryan, Brown & Company after the names of its founders, Alvin Bryan and George Warren Brown, and was incorporated 1881 as Bryan-Brown Shoe Company. In 1895, the company changed its name to the Brown Shoe Company. The company went bankrupt in 1939, but was able to successfully reorganize and continue business anchored by increasing demand for shoes by the Army and others as World War II progressed.[64] In the 1950s, the company began to diversify into shoe wholesaling and

63. *Id*. at 346.

64. *See Old Shoe Firm Bankrupt*, N.Y. TIMES, June 23, 1939, at 39; *Army Shoe Prices 20 to 37% Higher*, N.Y. TIMES, Dec. 10, 1940, at 46; *Army Shoe Orders Given 25 Concerns*, N.Y. TIMES,

retailing, acquiring Wohl Shoes in 1950 and Regal Shoes in 1953. Brown acquired G.R. Kinney Corporation in 1956, only to divest it to F.W. Woolworth, the nation's largest variety store, in 1963 for $39 million following the Supreme Court's decision.[65] Beginning in 1970s, Brown began closing its manufacturing plants, largely in response to import competition, and closed its last factories in 1995.[66] In 2015, Brown Shoe changed its name to Caleres, Inc. Today, the company is a global footwear retailer and wholesaler with annual net sales of $2.6 billion and approximately 12,000 full-time and part-time employees.[67] It operates Famous Footwear, one of America's leading family-branded footwear retailers, with 1,055 stores at the end of 2016 and net sales of $1.6 billion in 2016.[68]

UNITED STATES V. PHILADELPHIA NATIONAL BANK (1963).[69] In *United States v. Philadelphia National Bank*, one of the most important cases in antitrust law, the Supreme Court held that the plaintiff can make a prima facie showing of the requisite anticompetitive effect of a horizontal acquisition through an evidentiary presumption where the combined share of the merging firms is sufficiently high and the merger significantly increases market concentration:

> [A] merger which produces a firm controlling an undue percentage of the relevant market, and results in a significant increase in the concentration of firms in that market, is so inherently likely to lessen competition substantially that it must be enjoined in the absence of evidence clearly showing that the merger is not likely to have such anticompetitive effects.[70]

The *Philadelphia National Bank* Court did not fix numerical figures for invoking this presumption. In *Philadelphia National Bank* itself, however, the Court found the presumption established when the merging firms combined held over 30% of a

Dec. 20, 1940, at 47; *Army Purchases Shoes*, N.Y. TIMES, Mar. 2, 1941, at F7; *Army Places Big Shoe Orders*, N.Y. TIMES, Oct. 22, 1942, at 36.

65. *See Kinney Corp. Sold to Woolworth*, N.Y. TIMES, Sept. 4, 1963, at 57.

66. *See, e.g.*, *4 Shoe Plants in Missouri to Close*, N.Y. TIMES, Aug. 24, 1991, at 40; *Brown Group Unit Will Close 3 Plants, Dismiss Over 1,150*, WALL ST. J., Jan. 9, 1992, at B8; Isabelle Sender, *Brown Factory Closings Lead to $8.4M Qtr. Loss*, FOOTWEAR NEWS, Sept. 11, 1995, at 1 (reporting on closing of last five factories).

67. *See* Caleres, Inc., Form 10-K for the fiscal year ended January 28, 2017, at 4 (filed Mar. 28, 2017).

68. *Id*.

69. 374 U.S. 321 (1963), *rev'g* 201 F. Supp. 348 (E.D. Pa. 1962). For modern commentary on *Philadelphia National Bank,* see, for example, *An Interview with Judge Richard Posner*, 80 ANTITRUST L.J. 205 (2015); Peter C. Carstensen, *The Philadelphia National Bank Presumption: Merger Analysis in an Unpredictable World*, 80 ANTITRUST L.J. 219 (2015); Steven C. Salop, *The Evolution and Vitality of Merger Presumptions: A Decision-Theoretic Approach,* 80 ANTITRUST L.J. 269 (2015); Douglas H. Ginsburg & Joshua D. Wright, *Philadelphia National Bank: Bad Economics, Bad Law, Good Riddance*, 80 ANTITRUST L.J. 377 (2015); Daniel A. Crane, *Balancing Effects across Markets*, 80 ANTITRUST L.J. 397 (2015).

70. *Philadelphia Nat'l Bank*, 374 U.S. at 363.

relevant market in which the combined market share of the largest two firms increased from 44% to 59%.[71]

Philadelphia National Bank
Corporate Headquarters

On February 25, 1961, the Department of Justice filed a civil suit to enjoin the proposed merger of The Philadelphia National Bank ("PNB") and Girard Trust Corn Exchange Bank ("Girard"). The complaint charged that the acquisition may tend substantially to lessen competition in commercial bank services in the four-county Philadelphia metropolitan region in violation of Section 1 of the Sherman Act and Section 7 of the Clayton Act and sought to enjoin the transaction. PNB was a national bank with assets in excess of $1 billion and the second largest commercial bank in the four-county region. Girard was a state bank with assets of over $750 million and the third largest commercial bank in the area. PNB and Girard, which were both headquartered in Philadelphia, accounted for 21% and 16.1%, respectively, of the total commercial bank deposits in the four-county area.[72] If the merger was consummated, the resulting bank would become the largest in the area, with 37.1% of the area's total bank assets.[73] As a result of the merger, the two-firm concentration ratio in total bank assets would rise from 43.9% to 59%, and the four-firm concentration would rise from ___% to 77%.[74]

The government's case at trial was straightforward. The Justice Department relied principally on statistical market share evidence. The Department also introduced testimony by economists and bankers that, notwithstanding the extensive degree of federal and state regulation of the banking industry, there remained substantial areas where product availability, price and quality were determined by

Girard Trust Corn Exchange Bank
Main office

71. *Id*. at 364.

72. *Philadelphia Nat'l Bank*, 201 F. Supp. at 366.

73. *Id*. For some reason, the Supreme Court's opinion reports this share as 36%. *See* Philadelphia Nat'l Bank, 374 U.S. at 331.

74. *Id*. I have not yet been able to find or calculate the premerger four-firm concentration ratio.

competitive forces; that concentration in commercial banking, which the proposed merger would increase, would reduce these competitive forces; that the "area of the country" in which the competitive effect of the merger would be felt primarily would be the area in which the merging parties had their offices and branches, that is, a four-county area around Philadelphia; and that the relevant "line of commerce" was commercial banking. PNB and Girard responded by introducing contrary evidence on these propositions, as well as evidence that the merger was justified because the resulting bank would be better able to compete with out-of-state (particularly New York) banks, would attract new business to Philadelphia, and would generally promote the economic development of the region.

After a trial on the merits, the district court found that commercial banking was a proper relevant product market, but that the four-county metropolitan area was not a relevant geographic market because of competition with other banks for bank business throughout the greater northeastern United States. The district court also found that, even if the four-county region was an appropriate "area of the country" for merger antitrust analysis, there was no reasonable probability that the challenged transaction would substantially lessen competition among commercial banks in that area. Finally, the court found that the merger would benefit the Philadelphia metropolitan area economically. Accordingly, the district court dismissed the complaint.

The government appealed directly to the Supreme Court under the Expediting Act. In a six-to-two decision, the Supreme Court reversed, holding that the merger would violate Section 7 of the Clayton Act, and remanded the case with instructions to the district court to enter judgment enjoining the combination.[75] Justice William J. Brennan, Jr., wrote the opinion for the six-member majority.[76]

Product market definition presented "no difficulty" for the Court. With virtually no analysis, the Court agreed with the district court that "the cluster of products (various kinds of credit) and services (such as checking accounts and trust administration) denoted by the term 'commercial banking' composes a distinct line of commerce."[77] The Court devoted more attention to the question of geographic market definition. Here, the Court departed from the conclusion of the district court that the northeastern United States was the relevant area of the country. In an oft-quoted passage, the Court observed that "the proper question" to be asked is "not where the parties to the merger do business or even where they compete, but where, within the area of competitive overlap, the effect of the merger on competition will be direct and immediate."[78] This "area of effective competition" is determined as much by where existing purchasers can turn for supplies as by the trade area in which

75. The Court reserved the question of whether the combination also violated Section 1 of the Sherman Act.

76. Justice John Marshall Harlan, joined by Justice Potter Stewart, dissented. Justice Byron White did not participate.

77. *Philadelphia Nat'l Bank*, 374 U.S. at 356.

78. *Id*. at 357 (citing BETTY BOCK, MERGERS AND MARKETS 42 (1960)).

the parties operate.[79] The Court found that convenience of location is essential in banking, and consequently that inconvenience localizes competition in banking the same way that high transportation costs localize competition in other industries.[80] The Court then quickly leaped from the statement of these rules to the conclusion that the relevant geographic market was the four-county metropolitan area, where the "vast bulk" of both PNB's and Girard's business originated.

Having defined the product and geographic dimensions of the relevant market, the Court turned to the merger's expected effect on competition. The Court observed:

> Clearly, this is not the kind of question which is susceptible of a ready and precise answer in most cases. It requires not merely an appraisal of the immediate impact of the merger upon competition, but a prediction of its impact upon competitive conditions in the future; this is what is meant when it is said that the amended § 7 was intended to arrest anticompetitive tendencies in their "incipiency." Such a prediction is sound only if it is based upon a firm understanding of the structure of the relevant market; yet the relevant economic data are both complex and elusive. And unless businessmen can assess the legal consequences of a merger with some confidence, sound business planning is retarded. So also, we must be alert to the danger of subverting congressional intent by permitting a too-broad economic investigation. And so in any case in which it is possible, without doing violence to the congressional objective embodied in § 7, to simplify the test of illegality, the courts ought to do so in the interest of sound and practical judicial administration.[81]

Balancing these concerns, the Court concluded "in certain cases . . . elaborate proof of market structure, market behavior, or probable anticompetitive effects" was unnecessary and unwarranted.[82] Instead, given that the dominant theme motivating the Celler-Kefauver Act was an "intense congressional concern" over "a rising tide of economic concentration in the American economy,"[83] the Court held the requisite anticompetitive effect could be presumed from the changes in the market share distribution:

> Specifically, we think that a merger which produces a firm controlling an undue percentage of the relevant market, and results in a significant increase in the concentration of firms in that market, is so inherently likely to lessen competition substantially that it must be enjoined in the absence of evidence clearly showing that the merger is not likely to have such anticompetitive effects.[84]

The Court noted that this presumption is "fully consonant with economic theory": "That '[c]ompetition is likely to be greatest when there are many sellers, none of

79. *Id*. at 359 (citing Tampa Electric Co. v. Nashville Coal Co., 365 U.S. 320, 327 (1961)).

80. *Id*. at 358-59 (citing Crystal Sugar Co. v. Cuban-American Sugar Co., 152 F. Supp. 387, 398 (S.D.N.Y. 1957), *aff'd*, 259 F.2d 524 (2d Cir. 1958)).

81. *Id*. at 362 (citations omitted).

82. *Id*. at 363.

83. *Id*.

84. *Id*. (citing United States v. Koppers Co., 202 F. Supp. 437 (W.D. Pa. 1962)).

which has a significant market share,' is a common ground among most economists, and was undoubtedly a premise of congressional reasoning about the antimerger statute."[85]

Without establishing a hard and fast threshold, the Court held that PNB and Girard's combined market share of "at least 30%" was "undue," and that an increase in the two-firm concentration ratio from 44% to 59% represented a "significant increase" in market concentration, so that the presumptive rule of illegality was triggered.[86] The Court observed in a footnote[87] that Carl Kaysen and Donald Turner recommended in their seminal work that a combined 20% share should be the threshold of prima facie unlawfulness,[88] George Stigler also would employ a 20% threshold,[89] Jesse Markham would use a 25% test,[90] and Derek Bok would look primarily to changes in market concentration of 7% or 8%.[91] The Supreme Court observed that since a 30% combined share presents a "clear" threat to competition it was unnecessary to specify a minimum threshold, and emphasized that mergers resulting in a firm with less than 30% could nonetheless violate Section 7.[92]

Although the *Philadelphia National Bank* Court stressed that a presumption of anticompetitive effect based on market shares was rebuttable, with the acquiescence if not encouragement, of the Supreme Court, the lower courts rapidly transformed that rather mechanical presumption into a conclusive evidentiary inference. As a result, for years market definition—from which the market shares and market concentrations would be derived—was the battleground on which antitrust

85. *Id*. (internal citations and footnote omitted). To support the basic economic proposition, the Court cited JOE S. BAIN, BARRIERS TO NEW COMPETITION 27 (1956); CARL KAYSEN & DONALD TURNER, ANTITRUST POLICY 133 (1959); FRITZ MACHLUP, THE ECONOMICS OF SELLERS' COMPETITION 84-93, 333-36 (1952); Derek Bok, *Section 7 of the Clayton Act and the Merging of Law and Economics*, 74 HARV. L. REV. 226, 308-16, 328 (1960); Jesse M. Markham, *Merger Policy under the New Section 7: A Six-Year Appraisal*, 43 VA. L. REV. 489, 521-22 (1957); Edward S. Mason, *Market Power and Business Conduct: Some Comments*, 46 AM. ECON. REV. 471 (1956); George Stigler, *Mergers and Preventive Antitrust Policy*, 104 U. PA. L. REV. 176, 182 (1955). *See Philadelphia Nat'l Bank*, 374 U.S. at 363 nn.38-39, 364 n.41.

86. *Philadelphia Nat'l Bank*, 374 U.S. at 364 ("Without attempting to specify the smallest market share which would still be considered to threaten undue concentration, we are clear that 30% presents that threat.").

87. *Id*. at 364 n.41.

88. CARL KAYSEN & DONALD TURNER, ANTITRUST POLICY 133 (1959).

89. George Stigler, *Mergers and Preventive Antitrust Policy*, 104 U. PA. L. REV. 176, 182 (1955).

90. Jesse M. Markham, *Merger Policy under the New Section 7: A Six-Year Appraisal*, 43 VA. L. REV. 489, 522 (1957).

91. Derek Bok, *Section 7 of the Clayton Act and the Merging of Law and Economics*, 74 HARV. L. REV. 226, 328-29 (1960). Actually, in his published article Bok recommended 5% as a threshold. *Id*.

92. *Philadelphia Nat'l Bank*, 374 U.S. at 364 n.41 ("Needless to say, the fact that a merger results in a less-than-30% market share, or in a less substantial increase in concentration than in the instant case, does not raise an inference that the merger is not violative of § 7.").

challenges were fought, making *Philadelphia National Bank* the critical case for results, if not theory.

NOTES

1. Richard Posner, Brennan's law clerk during the 1962-63 term, reports that he wrote Brennan's opinion for the majority in *Philadelphia National Bank*.[93] Posner said that Brennan "wasn't very interested in the details of legal analysis, so we law clerks wrote the opinions and he would go over them."[94] While on the Harvard Law Review, Posner had been assigned to cite check a portion of a path-breaking article by Derek Bok entitled *Section 7 of the Clayton Act and the Merging of Law and Economics* in which Bok had argued for a simplified approach to Section 7 cases.[95] In *Philadelphia National Bank*, Posner incorporated the idea of a simple prima facie showing of anticompetitive effect in what is now known as the *PNB* presumption.

After clerking for Justice Brennan, Posner served from 1963 to 1965 as an attorney-advisor to FTC Commissioner Philip Elman. For the next two years, Posner was an assistant to Solicitor General Thurgood Marshall. Posner joined the faculty of the Stanford Law School in 1968 as an associate professor and moved to the University of Chicago Law School as a professor in 1969. In 1981, Posner was nominated by President Ronald Reagan to be a judge on the Court of Appeals for the Seventh Circuit, where he served as chief judge from 1993 to 2000.

UNITED STATES V. ALUMINUM CO. OF AMERICA (ROME CABLE) (1964).[96] On April 1, 1960, the Department of Justice filed a civil complaint charging that the acquisition by the Aluminum Company of America (Alcoa) of Rome Corporation violated Section 7 of the Clayton Act. Alcoa was a fully integrated aluminum producer. It was the nation's largest refiner of aluminum ore into primary aluminum, accounting for about 38% of total U.S. primary aluminum production capacity. It also manufactured a wide variety of intermediate and final aluminum products, including aluminum wire and cable. Alcoa made no copper products. Rome was primarily engaged in the manufacture of copper wire and cable products, although in 1952 it began making aluminum rod from aluminum ingot purchased from primary producers. Still, at the time of the acquisition, over 90% of Rome's production was of insulated copper products. Alcoa acquired Rome on March 31, 1959, in a stock exchange valued at the time at about $32 million.[97] The complaint alleged that the acquisition would substantially lessen actual and potential competition in "various

93, *See* Interview with Richard Posner, Securities and Exchange Commission Historical Society Oral History Project 2 (Jan. 25, 2011). A fuller account is provided in *An Interview with Judge Richard Posner*, 80 ANTITRUST L.J. 205, 218 (2015).

94. *Id*. at 2.

95. *See* Derek C. Bok, *Section 7 of the Clayton Act and the Merging of Law and Economics*, 74 HARV. L. REV. 226 (1960).

96. 377 U.S. 271 (1964), *rev'g* 214 F. Supp. 501 (N.D.N.Y. 1963) (Blue Book No. 1512).

97. *See Court in Antitrust Case Clears Alcoa Purchase of Rome Cable*, N.Y. TIMES, Jan. 30, 1963, at 12.

wire and cable products" generally and between Alcoa and Rome in particular, and sought an order of divestiture and an injunction against further acquisitions of any company engaged in the production or sale of wire or cable products, conduit, or cable accessories.

After a four-week trial on the merits, the district court held that the acquisition did not violate Section 7 and dismissed the complaint. Product market definition was the central issue. The district court found that aluminum wire and cable were used almost exclusively by electric utilities for electric power transmission. Copper wire was also used for this purpose. In overhead lines, bar or lightly insulated aluminum conductor had virtually displaced copper conductor in new installations. Underground, however, where the conductor has to be heavily insulated, copper was by far the dominant conductor. The district court found that bare aluminum conductor was a separate line of commerce, but that insulated aluminum conductor had to be included in the same relevant market with insulated copper conductor. The court rejected an all-aluminum conductor product market on the grounds that insulated cooper conductor had to be included in any market containing insulated aluminum conductor.[98] Within the two relevant markets found by the court—bare aluminum conductor and insulated aluminum plus copper conductor—the shares of the merging companies and the change in concentration resulting from the merger were not sufficiently high to warrant antitrust concern.

Alcoa/Rome Shares in Various Proposed Product Markets

Proposed lines of commerce	Alcoa Share	Alcoa Rank	Rome Share	Rome Rank	Combined Share	Combined Rank	D.C. Result
Bare aluminum conductor	32.5%		0.3%		32.8%		No violation
Insulated aluminum conductor	11.6%	3	4.7%	8	16.3%		No market
Insulated aluminum and copper conductor	0.3%		1.3%		1.6%		No violation
Aluminum conductor (bare and insulated)	27.8%	1	1.3%	9	29.1%	1	No market
All conductor	1.8%		1.4%		3.2%		No violation

98. *Alcoa*, 214 F. Supp. at 510.

Note: Blank cells indicate that the data was not contained in the court's opinion

The district court made three other findings that supported its dismissal of the complaint. First, the court found that Alcoa's purpose in acquiring Rome was to gain expertise in the manufacture of more sophisticated types of insulated aluminum conductor and not to eliminate a competitor. Indeed, the court found that Alcoa and Rome competed in only four products and that Rome's production in the overlapping products was not significant.[99] Second, although the government argued that concentration in the aluminum *industry* was increasing, the court found that concentration in aluminum *conductors* was decreasing. Moreover, prior to the Rome acquisition, Alcoa had not acquired any companies involved in the manufacture or sale of aluminum conductor. Third, the court found that there was ease of entry into the manufacture and sale of aluminum conductor and that in the preceding ten years the number of insulated aluminum conductor manufacturers grew from four to twenty-nine (most of which, like Rome, were originally insulated copper conductor manufacturers). The court noted that several manufacturers had exited the business for failure to make a profit, indicating that the business was operating competitively.

On a direct appeal under the Expediting Act, the Supreme Court reversed in a six-to-three decision. Justice William O. Douglas wrote the majority opinion. Douglas focused immediately on the district court's rejection of an all-aluminum conductor market. Douglas agreed that there is competition generally between insulated aluminum conductor and insulated copper conductor. But in overhead distribution, Douglas found, insulated aluminum conductor has "decisive advantages" over insulated copper conductor—including its costs being 50% to 65% of the cost of insulated copper conductor—and that its share of total installations increased from 6.5% in 1950 to 77.2% in 1959.[100] Douglas found that these facts justified making insulated aluminum conductor its own "submarket." Without further analysis, Douglas also held that it was "proper" to combine bare and insulated aluminum conductor into a single "all aluminum conductor" market, presumably on the view that it is permissible to combine two lines of commerce into a new single market.[101]

Douglas found that the Alcoa/Rome transaction violated Section 7 in an all-aluminum conductor market. Douglas observed that the all-aluminum conductor market was highly concentrated, with Alcoa as the largest producer, Alcoa and Kaiser Aluminum & Chemical Corporation controlling 50% of the market, and the largest five firms controlling more than 76% of the market. Quoting *Philadelphia National Bank*, Douglas noted that "if concentration is already great, the importance of preventing even slight increases in concentration and so preserving the possibility of eventual deconcentration is correspondingly great."[102] Douglas concluded:

99. *Id*. at 512.

100. *Alcoa*, 377 U.S. at 276.

101. *Id*. at 276-77.

102. *Id*. at 279 (quoting United States v. Philadelphia Nat'l Bank, 374 U.S. 321, 365 n.42 (1963)).

> The acquisition of Rome added, it is said, only 1.3% to Alcoa's control of the aluminum conductor market. But in this setting that seems to us reasonably likely to produce a substantial lessening of competition within the meaning of § 7. It is the basic premise of that law that competition will be most vital "when there are many sellers, none of which has any significant market share." *United States v. Philadelphia National Bank*, 374 U. S., at 363. It would seem that the situation in the aluminum industry may be oligopolistic. As that condition develops, the greater is the likelihood that parallel policies of mutual advantage, not competition, will emerge. That tendency may well be thwarted by the presence of small but significant competitors. Though percentagewise Rome may have seemed small in the year prior to the merger, it ranked ninth among all companies and fourth among independents in the aluminum conductor market; and in the insulated aluminum field it ranked eighth and fourth respectively. Furthermore, in the aluminum conductor market, no more than a dozen companies could account for as much as 1% of industry production in any one of the five years (1955-1959) for which statistics appear in the record. Rome's competition was therefore substantial. The record shows indeed that Rome was an aggressive competitor. It was a pioneer in aluminum insulation and developed one of the most widely used insulated conductors. Rome had a broad line of high-quality copper wire and cable products in addition to its aluminum conductor business, a special aptitude and skill in insulation, and an active and efficient research and sales organization. The effectiveness of its marketing organization is shown by the fact that after the merger Alcoa made Rome the distributor of its entire conductor line. Preservation of Rome, rather than its absorption by one of the giants, will keep it "as an important competitive factor," to use the words of S. Rep. No. 1775, [81st Cong., 2d Sess.] p. 3 [1950]. Rome seems to us the prototype of the small independent that Congress aimed to preserve by § 7.[103]

The Court reversed the judgment of the district court and remanded with instructions to fashion an appropriate divestiture decree.

Justice Potter Stewart, joined by Justices John M. Harlan and Arthur J. Goldberg, dissented. First, Stewart argued that the district court's "practical judgment," based on a pragmatic application of the *Brown Shoe* factors, that insulated aluminum conductors were not a relevant line of commerce should be sustained.[104] Second, even if insulated aluminum conductors were a relevant line of commerce, Stewart argued, the evidence showed that bare aluminum conductor and insulated aluminum conductor did not compete with one another and that it was improper to include them in the same relevant market. [105]

UNITED STATES V. VON'S GROCERY CO. (1966).[106] On January 25, 1960, Von's and Shopping Bag Food Stores agreed to merge effective March 28, 1960 in a stock-

103. *Id.* at 280-81.

104. *Id*. at 284 (Stewart, J., dissenting).

105. *Id*. at 286.

106. 384 U.S. 270 (1966), *rev'g* 233 F. Supp. 976 (S.D. Cal. 1964) (Blue Book No. 1510).

for-stock transaction.[107] Von's operated 28 supermarkets in the Los Angeles area with total annual sales of approximately $85 million, yielding an average of approximately $3 million in sales per store. Shopping Bag operated 36 supermarkets in the area with total annual sales of approximately $79 million for an average of approximately $2.1 million in sales per store. In 1958, Von's ranked third and Shopping Bag Food Stores fifth in terms of total sales by grocery stores in the Los Angeles metropolitan area; Von's had approximately a 4.7% share and Shopping Bag approximately a 4.2% share. After the merger, the combined company would be the largest retail grocery chain in the Los Angeles area with a share of 8.9%.[108]

On March 25, 1960, three days before the effective date of the merger, the Department of Justice filed a civil complaint charging that the proposed merger violated Section 7 of the Clayton Act. The complaint alleged that the acquisition would substantially lessen competition in the purchase, distribution, and sale of groceries and related products in the Los Angeles area. The complaint also alleged that Von's competitive advantage over smaller sellers of groceries might be enhanced by the merger and that independent retailers might be deprived of a fair opportunity to compete with the combined firm. The government sought a preliminary injunction to block the closing pending an adjudication of the merits and a permanent injunction to block the transaction altogether.

The Department did not fare well in the district court. On March 28, the court denied the Department's application for a temporary restraining order (TRO) and allowed the merger to proceed. On June 3, 1960, the court denied the government's application for a preliminary injunction to require Von's and Shopping Bag to be operated as separate entities pending trial of the action. On December 15, the court denied the Department's motion for summary judgment, and on September 14, 1964, following a trial on the merits largely on a stipulated record, the court found for the defendants and dismissed the complaint.

Since the parties agreed both that the retail sale of groceries and related products was the relevant product market and that the Los Angeles metropolitan area was the relevant geographic market,[109] the only question for the court was the merger's

107. *See Merger Plans Approved By Von's Grocery, Shopping Bag Boards*, WALL ST. J., Jan. 27, 1960, at 13; *Von's Grocery, Shopping Bag Plan Merger*, L.A. TIMES, Jan. 27. 1960, at 23; *Shopping Bag, Von's Grocery Merger Voted*, L.A. TIMES, Mar. 18, 1960, at C10.

108. *Von's*, 233 F. Supp. at 980. The Supreme Court found the combined share to be 7.5% and the combined firm to be the second largest grocery retailer in the Los Angeles area. *See Von's*, 384 U.S. at 272.

109. *Id*. at 979.

probable effect on competition. The district court found that the market was characterized by ease of entry and was very competitive:

> In 1960, the approximately 4,800 stores in the area were operated by 4,000 separate concerns. During 1960, 128 new "single outlet" stores opened. The leading 20 chains opened 67 new stores in 1960 against 171 by smaller chains and single store operators. While the 10 leading chains accounted for 43.6%, the remainder, including 3,818 single store operators, accounted for 56.4% of the sales in the area in 1960. Another indication of the competitive situation is the fact that Shopping Bag's gross increased while its profits decreased. The witness, Hayden, president of the company, testified that this was occasioned by competition as well as the need for experienced executives.[110]

The court also noted the role of cooperatives, which allowed smaller stores to achieve the same volume purchasing discounts as the larger chains and which had open membership. Overall, the court found that the average shopper had from two to ten competing stores within convenient distance to shop and that competition, even after the merger, had driven prices down "about as far as possible."[111] The court concluded that the acquisition would have no likely adverse effect on competition:

> The government argues that over-all competition has been substantially reduced by the merger, but the proof falls short of establishing such to be the case. In fact, the figures relied upon by the government tend to establish to the contrary. Again it is repeated that in 1960 the approximately 4,800 stores in the area were operated by 4,000 separate concerns. The merger here did not materially change that situation. It did not increase or decrease competition store for store with any grocer, single store, or chain, since the acquired stores continued as before. As between stores, only a few of those of Von's and Shopping Bag were in direct competition since generally each company's stores were in different localities of the area. A few did compete directly. Apparently the reason for the failure of the evidence to pinpoint a decrease in competition was because there was actually no decrease.[112]

The government appealed directly to the Supreme Court under the Expediting Act. In a six-to-two decision, the Supreme Court reversed and remanded with instructions to the district court to enter a divestiture order. In an opinion by Justice Hugo L. Black, the Court quickly summarized the facts supporting its conclusion. Von's and Shopping Bag were respectively the third and sixth largest retail grocery stores in the Los Angeles area. Together, they became the second largest retail grocery retailer in the Los Angeles area, with a share of 7.5%. Prior to the merger, both were "rapidly growing" and "highly successful."[113] At the same time, the number of owners operating single stores in the market had decreased from 5,365 in 1950 to 3,818 in 1961, and finally to 3,590 in 1963. Many of the single stores were

110. *Id*. at 982.

111. *Id*. at 985.

112. *Id*. at 983-84.

113. *Von's*, 384 U.S. at 272.

being acquired by chains. Between 1949 and 1958, nine of the top twenty chains acquired 126 stores from their smaller competitors. Overall, the number of chains with two or more stores increased from 96 in 1953 to 150 in 1962. Although not part of the record, Black noted a table prepared by the FTC and included in the government's reply brief that mergers and acquisitions had "continued at a rapid rate since the merger."[114] Black concluded: "These facts alone are enough to cause us to conclude contrary to the District Court that the Von's-Shopping Bag merger did violate § 7. Accordingly, we reverse."[115]

Black's opinion makes clear that the majority read the purpose of the Clayton Act following the Celler-Kefauver amendments was to arrest the "'rising tide' toward concentration into too few hands and to halt the gradual demise of the small businessman."[116] Although Black mentioned in passing that the combined company accounted for 7.5% of the grocery sales in the Los Angeles area, he never used this figure in his analysis. Nor did Black mention any concentration ratios in his opinion or make reference to, much less employ, the *PNB* presumption. To the majority, the key fact was that the number of single store operators was declining. While some single operators may have exited the market altogether because of inefficiency or mismanagement, others were acquired by larger chains.[117] Black concluded:

> It is enough for us that Congress feared that a market marked at the same time by both a continuous decline in the number of small businesses and a large number of mergers would slowly but inevitably gravitate from a market of many small competitors to one dominated by one or a few giants, and competition would thereby be destroyed. Congress passed the Celler-Kefauver Act to prevent such a destruction of competition.[118]

Justice Potter Stewart, joined by Justice John M. Harlan, issued a vigorous dissent. Stewart noted that *Brown Shoe* had established two fundamental principles in applying Section 7: acquisitions were to be judged light of economic context of their industry and contemporary economic theory, and the purpose of Section 7 is to protect competition, not competitors. But, Stewart observed, the majority performed no analysis of the competitive effects of the acquisition and instead applied Section 7. Expanding upon the district court's analysis, Stewart concluded that any

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114. *Id*. at 274. The table, reprinted as Appendix 2 to the majority opinion, show that 134 stores had been acquired by twelve companies between 1961 and 1964. *See id.* at 280.

115. *Id*.

116. *Id*. at 276; *see id.* at 275 ("[T]he basic purpose of the 1950 Celler-Kefauver Act was to prevent economic concentration in the American economy by keeping a large number of small competitors in business.") (footnote omitted).

117. Using the numbers supplied in the Court's opinion, there were 547 fewer single store operators in the market in 1961 than there were in 1950. During roughly the same time period (1949 to 1948), nine of the top twenty chains acquired 126 stores from their smaller competitors. Assuming that these nine companies accounted for most of the acquisitions and assuming no entry into the market (certainly not correct), in the neighborhood of 75% of the single store operators shut down their stores rather than sold them to an acquirer.

118. *Id*. at 278.

competitive analysis of Los Angeles retail grocery sales would reveal vigorous competition, an unconcentrated market, no trend forward concentration, considerable new entry, and substantial movement over time in the identities of many of the larger chains. Moreover, Stewart noted that, for the most part, Von's stores were located in the southern and western areas of Los Angeles and that Shopping Bag stores were located in the northern and eastern areas. Where Von's and Shopping Bag stores did compete directly, the record showed that there were also other chain stores and several smaller stores competing for the patronage of the same customers.[119] With respect to small grocers, Stewart concluded that they were in need of no protection. Stewart observed that they were thriving in Los Angeles, cooperative purchasing groups ensured that they could purchase at prices competitive with the large chains, and the most aggressive competitors were frequently single store operators. Stewart also observed that there are no substantial barriers to entry into the Los Angeles retail grocery market and that numerous new small firms had entered. Stewart pointedly noted that the majority did not and could not invoke the *PNB* presumption: "[T]he circumstances of the present merger fall far outside the simplified test established by that case for precisely the sort of merger here involved."[120] Stewart would have sustained the dismissal of the case by the district court.

NOTES

1. *Von's* is considered by most to be the poster child for aggressive antitrust restrictions on low market share horizontal transactions in unconcentrated markets. Interestingly, the argument in the Supreme Court for this aggressive position was made by Richard A. Posner.

UNITED STATES V. PABST BREWING CO. (1966).[121] On July 30, 1958, Pabst Brewing Company acquired the assets and business of Blatz Brewing Company from Schenley Industries, Inc. in a deal valued at about $14.5 million.[122] At the time of the acquisition, Pabst ranked tenth in sales of beer in the United States with 3.02% of the nationwide beer sales and operated four breweries: Milwaukee, Wisconsin, Peoria Heights, Illinois, Newark, New Jersey, and Los Angeles, California. Blatz ranked eighteenth with 1.47% of nationwide bee sales and operated one brewery in Milwaukee, Wisconsin. Following the acquisition, the Blatz brewery was closed and Blatz brand beer was brewed in the four Pabst plants.

A little over a year later, on October 1, 1959, the Department of Justice filed a civil complaint charging that the acquisition violated Section 7 of the Clayton Act. The complaint alleged that the effect of the acquisition may be substantially to lessen competition or to tend to create a monopoly in the production and sale of beer in the

119. *Id*. at 295-96 (Stewart, J., dissenting).

120. *Id*. at 302 (footnote omitted).

121. 384 U.S. 546 (1966), *rev'g* 233 F. Supp. 475 (E.D. Wis. 1964) (Blue Book No. 1479).

122. *Pabst Brewing Acquires Blatz From Schenley for 14.5 Million*, N.Y. TIMES, July 31, 1958, at 33.

United States, the State of Wisconsin, and the three state area of Wisconsin, Illinois and Michigan and sought a permanent injunction ordering Pabst to divest Blatz. Before trial, the parties stipulated that the relevant product market was the production, sale and distribution of beer and that the continental United States was a relevant geographic market. The issues for trial were whether the State of Wisconsin and the three state area of Wisconsin, Illinois and Michigan were also relevant geographic markets and whether the acquisition entailed a reasonable probability of a substantial lessening of competition in any properly defined relevant market.

The trial began on January 27, 1964. At 3:45 pm the next day, after offering 260 exhibits and reading portions of deposition testimony, the government rested.[123] Pabst then moved to dismiss under Rule 41(b) of the Federal Rules of Civil Procedure for failure to prove a prima facie case. After a full briefing and a hearing, the district court granted the motion and dismissed the complaint.

First, the district court held that the government failed to prove that either Wisconsin or the three state area of Wisconsin, Illinois and Michigan constituted a proper relevant market in which to analyze the competitive effects of the transaction. The government had argued that Wisconsin was a relevant market because (1) prior to the acquisition, the most intense competition between Pabst and Blatz existed in Wisconsin, and therefore the impact of the acquisition would be most severe in that state, (2) Wisconsin's standing in the beer industry made it an appreciable segment of the market, (3) each state was a separate relevant market, since each state has its own regulations affecting the beer industry, (4) Blatz prices were higher in Wisconsin than in any other state, and (5) Wisconsin's high per capita consumption of beer, high consumption of draught beer and large number of small, locally owned breweries made it a unique market. The government made analogous arguments for a Wisconsin-Illinois-Michigan relevant geographic market. The court, after a detailed analysis distinguishing the precedent cited by the government, rejected the two proposed markets because they did not reflect the "commercial realities" of the beer industry. Pabst and Blatz competed throughout most of the continental United States and

123. The district court was clearly perturbed by this development, since the government had told the court repeatedly that it intended to call 71 live witnesses at trial, resulting in several reschedulings to accommodate a long trial. Two days before the trial was to start, the government changed its position and told the court that it would take no more than two trial days to present its case and that it would offer no witnesses. *See Pabst Brewing*, 233 F. Supp. at 478-80.

nothing makes Wisconsin or the three state area distinct from the national beer market.

Second, the district court held that the government failed to prove a prima facie case of likely anticompetitive effects in the continental United States beer market, the only geographic market remaining in the case. The court held that the national market share of the combined company—4.79% in 1959 and 5.83% in 1961—was not by itself sufficient to predicate an "undue percentage of the relevant market" under the *PNB* presumption.[124] Moreover, the court found that the government failed to prove any trend toward concentration that Section 7 was intended to prevent. Significantly, after reviewing the precedent, the court held that only a trend toward concentration for Section 7 purposes was not merely a reduction in the number of competitors, but a reduction due to a history of acquisitions.[125] While the court acknowledged that the number of breweries had declined in the United States from 750 in 1934, to 264 in 1957, and finally to 229 in 1961, "[s]o far as the record discloses, not a single merger or acquisition in the beer industry preceded the acquisition of Blatz by Pabst and the decrease in the number of breweries resulted from the play of natural economic forces."[126] In light of the government's failure to prove a prima facie case of anticompetitive effect, the district court dismissed the complaint.

The government appealed directly to the Supreme Court under the Expediting Act. Although all nine justices voted to reverse, three of justice concurred only in the result.

Justice Black, the author of the majority opinion in *Von's*, again wrote the majority decision. First, Black held that the district court erred in failing to find that the government did prove a prima facie case that Wisconsin and Wisconsin-Michigan-Illinois were relevant geographic markets in which to assess the competitive effects of the transaction. Black gave short shrift to the question of geographic market definition. To Black, Section 7's requirement that the plaintiff prove a reasonable probable anticompetitive effect "in any section of the country" did not mean that the plaintiff had to prove an economically meaningful geographic market:

> The language of this section requires merely that the Government prove the merger may have a substantial anticompetitive effect somewhere in the United States "in *any* section" of the United States. This phrase does not call for the delineation of a "section of the country" by metes and bounds as a surveyor would lay off a plot of ground. 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. In either event a violation of § 7 would be proved. Certainly the failure of the Government to prove by an army of expert witnesses what constitutes a relevant

124. *Id*. at 491.

125. *Id*. at 492.

126. *Id*. at 493.

> "economic" or "geographic" market is not an adequate ground on which to dismiss a § 7 case. 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 any or all parts of the country. Proof of the section of the country where the anticompetitive effect exists is entirely subsidiary to the crucial question in this and every § 7 case which is whether a merger may substantially lessen competition anywhere in the United States.[127]

Without further analysis, Black sustained the government's proof of Wisconsin and Wisconsin-Michigan-Illinois as relevant "sections of the country" in which to analyze the competitive effects of the transaction.

Turning to competitive effects, Black reported the figures in the following two tables.

Pabst/Blatz

	Pabst		Blatz		Combined	
Section of the country	Share	Rank	Share	Rank	Share	Rank
Continental U.S. (1958)		10		18	4.49%	5
Continental U.S. (1961)					5.83%	3
Wis.-Mich.-Ill.	5.48%	7	5.84%	6	11.32%	
Wisconsin (1958)		4		1	23.95%	1
Wisconsin (1961)					27.41%	

Trend toward Concentration

	United States		Wis.-Mich.-Ill.		Wisconsin	
	Breweries	10-FCR	Breweries	8-FCR	Breweries	4-FCR
1934	714					
1955					77	
1957		45.06%	104	58.93%		47.74%
1961	229	52.60%	86	67.65%	54	58.62%

Black concluded:

> These facts show a very marked thirty-year decline in the number of brewers and a sharp rise in recent years in the percentage share of the market controlled by the leading brewers. If not stopped, this decline in the number of separate competitors and this rise in the share of the market controlled by the larger beer

127. *Pabst Brewing*, 384 U.S. at 549-50 (emphasis in original; internal citation and footnote omitted).

> manufacturers are bound to lead to greater and greater concentration of the beer industry into fewer and fewer hands. . . . In accord with our prior cases, we hold that the evidence as to the probable effect of the merger on competition in Wisconsin, in the three state area, and in the entire country was sufficient to show a violation of § 7 in each and all of these three areas.[128]

In reaching this result, Black rejected the district court's view that Section 7 was only concerned about a trend toward concentration due to mergers:

> Congress, in passing § 7 and in amending it with the Celler-Kefauver Anti-Merger amendment, was concerned with arresting concentration in the American economy, whatever its cause, in its incipiency. To put a halt to what it considered to be a "rising tide" of concentration in American business, Congress, with full power to do so, decided "to clamp down with vigor on mergers." . . . We hold that a trend toward concentration in an industry, whatever its causes, is a highly relevant factor in deciding how substantial the anti competitive effect of a merger may be.[129]

Justice Harlan, joined by Justice Stewart, concurred in the result.[130] While Harlan agreed that the government had made out a prima facie case that Wisconsin and Wisconsin-Michigan-Illinois are proper "sections of the country" in which to analyze the Pabst/Blatz merger, they disagreed with Black that a "section of the country" within Section 7 could be something other than a meaningful economic market. Here, Harlan believed that the government had satisfied its burden of proof by presenting evidence that that "significant barriers exist to prevent outside brewers from entering the Wisconsin market as effective competitors to those brewers already marketing beer there."[131] Contrary to the majority, Harlan and Stewart would have sustained the district court's finding that failed to prove a prima facie case of the requisite anticompetitive effect in the continental United States market.

Justice Abe Fortas also concurred in result, agreeing with Harlan and Stewart that proof of an economically meaningful relevant geographic market is an essential element of a Section 7 case: "Unless both the product and the geographical market are carefully defined, neither analysis nor result in antitrust is likely to be of acceptable quality."[132]

UNITED STATES V. GENERAL DYNAMICS CORP. (1974).[133] In the ten or so years since *Philadelphia National Bank*, the *PNB* presumption had become conclusive. Moreover, given the flexibility of the courts in defining markets coupled with a strong tendency to accept the government's alleged markets, the *PNB* presumption could be triggered in almost every government case. As a practical matter, horizontal acquisitions by large companies even of small competitors became per se unlawful.

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128. *Id*. at 551-52 (footnote omitted).
129. *Id*. at 552-53 (citation omitted).
130. Recall that Justice Stewart, joined by Justice Harlan, dissented in *Von's*.
131. *Pabst Brewing*, 384 U.S. at 558 (Harlan, J., concurring in result).
132. *Id*.at 562 (Fortas, J., concurring in result).
133. 415 U.S. 486 (1974), *aff'g* 341 F. Supp. 534 (N.D. Ill. 1972) (Blue Book No. 1861).

In 1974, the Supreme Court dramatically changed the course of horizontal merger analysis with its decision in *General Dynamics*. Not only did the Court return the *PNB* presumption to its rebuttable roots, the Court also brought a new emphasis to the importance of non-market share factors probative of the competitive consequences of horizontal acquisitions. Notwithstanding market shares of 15.1% and 8.1% in the relevant market and a rapidly declining number of industry participants—more than enough to invoke the rule of presumptive illegality under *Von's* and the other post-*Philadelphia National Bank* cases—the Court permitted one coal producer to acquire a controlling interest in another coal producer. The Court found that the acquired company's coal reserves were already committed by long-term contracts to electric utilities at predetermined prices. Lacking a supply of uncommitted coal that could be sold in the future at terms and conditions of the acquired firm's choosing, the Court found that acquired firm no longer was a significant independent competitive force which could affect prices and output in the marketplace. Accordingly, not only was the presumption of likely anticompetitive effect unreliable in this case, on the evidence before it the Court found no likelihood that the acquisition would substantially lessen competition in the future.

In 1954, Material Service Corporation acquired 10 percent of the stock of United Electric Coal Companies, a coal strip and open-pit miner in Illinois and Kentucky. Material was a large midwest building materials producer and supplier of building materials, concrete and limestone. Through its wholly-owned mining subsidiary Freeman Coal Mining Corporation, Material operated four deep coal mines in southern and central Illinois. Material had never operated a strip mine and lacked the experience and experience to do so. During the next several years, Material increased its stock ownership in United Electric and by 1959 Material had acquired more than 34 percent of United Electric's outstanding stock. This stock interest provided Material with effective control of United Electric and from 1959 forward Freeman and United Electric were operated under common control.

Several months after the 1959 management reorganization, Material was acquired by General Dynamics Corporation. At the time, General Dynamics was a large diversified company with the bulk of its revenues coming from sales of aircraft, communications and marine products to various government defense agencies. General Dynamics acquired a majority interest in Material as part of a diversification program to enter non-defense commercial businesses. In the early 1960s General Dynamics continued to increase its holding in United Electric, and in 1966 obtained the remaining outstanding stock through a tender offer and squeeze-out merger.

Although all of these developments had been publicly disclosed—indeed, the Justice Department had been furnished information about Material's stock interests in United Electric in 1960—it was not until 1967 that the Antitrust Division commenced its Section 7 action against the Material's acquisition of effective control and against General Dynamics solidification of that control. The action sought permanent relief in the form of an order requiring General Dynamics to divest its interest in United Electric.

The government approached the case as a straightforward horizontal merger. Both Material and United Electric sold coal in Wisconsin, Illinois, Kentucky, Iowa, and Missouri. Indeed, about half of the coal sold by each company was shipped to common customers, virtually all of which were electric utilities. The complaint alleged that the relevant product market was coal, and that the relevant geographic market was the State of Illinois, or alternatively, the Eastern Interior Coal Province Sales Area (which included Illinois and Indiana, as well as parts of Kentucky, Tennessee, Iowa, Minnesota, Wisconsin, and Missouri), one of four major coal producing regions in the United States.

The government sought to prove that the acquisitions posed the requisite threat to competition for a Section 7 violation through the *PNB Bank* presumption. In 1959, Material accounted for 15.1% of Illinois coal production and 7.6% of the coal production in the Eastern Interior Coal Province, and was the second largest coal producer in each of these areas. United Electric's share was 8.1% in Illinois and 4.8% in the Eastern Province. By the time of trial in 1967, Material's coal production had dropped in Illinois to 12.9% and in the Eastern Province to 6.5%. Meanwhile, United Electric's share had increased slightly in Illinois to 8.9% and decreased slightly in the Eastern Province to 4.4%. The combination of Material and United Electric became the coal producer in Illinois in 1959 and the second largest in the Eastern Province.

At trial, the primary issues emerged: (1) the propriety of "coal" as the relevant product market; (2) the propriety of Illinois and the Eastern Interior Coal Sales Areas as the relevant product markets; and (3) the probability of any lessening of competition in the alleged relevant markets as a result of the acquisition of control over United Electric.

General Dynamics-Material/United Electric

Market	General Dynamics Share Rank	United Electric Share Rank	Combined Firm Share Rank	n-CR	Change Pts Δ%	Conc. Trend
			1959			
Illinois	15.1% 2	8.1% 5	23.2% 1	2: 37.8% 4: 54.5 10: 84.0	7.7 22.4%	Yes
Eastern Interior Coal Province	7.6% 2	4.8% 6	12.4% 2	2: 29.6% 4: 43.0 10: 65.5	4.8 14.5%	Yes
			1967			
Illinois	12.9% 2	8.9% 6	21.8% 2	2: 37.8% 4: 54.5 10: 84.0	7.7 22.4%	Yes
Eastern Interior Coal Province	6.5% 5	4.4% 9	10.9% 2	2: 29.6% 4: 43.0 10: 65.5	4.8 14.5%	Yes

Rank: Market rank
Pts: Point change in the n-CR
Conc. Trend: Trend toward concentration
n-CR: N-firm concentration ratio
Δ%: Percentage change in the n-CR

The district court rejected the government's proposed product market definition. It held, after an extensive discussion of the evidence, that interfuel competition between coal, oil, natural gas, and nuclear energy for electric utility supply contracts required that the relevant line of commerce for testing the competitive effect of the transaction to be the "energy market." The court also rejected the government's contention that coal was a relevant submarket, holding that such a submarket ignores what the buyers (almost exclusively electric utilities) actually do, that is, compare various forms of energy in making their purchasing decisions. The district court reasoned that if the competition between glass and metal containers was sufficient to include them both in the same relevant market, as the Supreme Court did in *Continental Can* over the opposition of the defendants, then coal and other forms of energy sources should also be included in the same relevant market.[134]

The district court also rejected the government's proposed geographic market definitions. The court observed that the government's proposed markets were based on production patterns, not consumption patterns, and that no customer of either Material or United Electric purchased, or that any producer sold, coal throughout either of the government's proposed markets. Instead, the court found that the cost of

134. *General Dynamics*, 341 F. Supp. at 555-56 (*citing as authority* United States v. Continental Can Co., 378 U.S. 441 (1964)).

transporting coal may approach 30% to 40% of its delivered price and is therefore a critical factor influencing the choice of coal suppliers that can realistically compete for a given utility's business. The evidence showed that mines located in Illinois, Indiana and western Kentucky long had been grouped into Freight Rate Districts designated by the Interstate Commerce Commission and that different rate districts serve a different and distinct geographic area.[135] Consequently, the court held that the relevant geographic markets in this case were eight Freight Rate Districts. The court also identified two individual customers to be relevant geographic markets. Commonwealth Edison, which has multiple facilities throughout the region, annually consumed a quantity of coal equal to the combined production of several freight rate districts and in fact purchases throughout multiple districts. Commonwealth Edison also had the most extensive commitment to the use of nuclear energy and had embarked on an air pollution reduction program that called for increasing use of nuclear energy, gas and oil. Similarly, the Metropolitan Chicago Intestate Air Quality Control Region had adopted air pollution control regulations that prohibited the burning of coal with high levels of sulfur content.

Although the district court found that the government's case was fatally deficient for failure to establish its alleged relevant markets, the district court further found that even if the government's proposed markets had been adopted the challenge would fail because of "the Government's failure to show that a substantial lessening of competition resulted from the United Electric-Freeman combination" in any product or geographic market.[136] This determination rested on three findings:

1. The decline in the number of coal producers in Illinois and in the Eastern Interior Coal Province occurred, not because of acquisitions by others, but as the inevitable result of the declining demand for coal as an energy source. This reduction in demand also was reflected in the fact that the combined company produced less coal in 1967 than it did in 1959. Accordingly, the court observed, the instant case is distinguishable from trend toward concentration resulting from mergers and acquisitions found in *Philadelphia National Bank* and *Von's* which justified preventing even slight increases in concentration.

2. Material and United Electric were "predominantly complementary in nature." United Electric was a strip mining company with no experience in deep mining nor any likelihood in acquiring it, while Material was a deep mining company with no experience or expertise in strip mining. Moreover, the mine and coal reserves of Material and United Electric were located in different freight rate districts. Finally, United Electric does not and cannot produce coal that meets the sulphur limits of the Metropolitan Chicago Intestate Air Quality Control Region. The only

135. The history and functions of the Freight Rate Districts in issue are discussed in Ayrshire Collieries Corp. v. United States,335 U.S. 573, 576 (1949).

136. *General Dynamics*, 341 F. Supp. at 557.

common sales in 1965-1967—the period chosen by the government for analysis—where to Commonwealth Edison.

3. The bulk of United Electric's existing reserves were either depleted or committed under long-term supply contracts and the prospect of obtaining new reserves was remote. Material had to use coal from one of its mines to discharge United Electric's obligations to Illinois Power Company when United Electric found its reserves inadequate. Several of United Electric's other long-term contracts were backed up by Material's reserves and could not have been obtained without this support. Nor could United Electric find new reserves. Evidence at trial, including testimony by government experts, showed that economically minable strip mine reserves were not presently available. Consequently, United Electric's ability to be a competitive force and affect the market price of coal was severely limited and steadily diminishing.

The district court concluded that, under these circumstances, the combination's continuation would not adversely affect competition nor would divestiture benefit competition. The court dismissed the government's complaint.

The government appealed directly to the Supreme Court under the Expediting Act. It sought to revive coal as a relevant line of commerce for antitrust analysis through a largely mechanical application of the *Brown Shoe* submarket indicia. Coal, the government argued, is recognized by the industry, governmental authorities, and the public as a separate economic entity. It is physically different from other forms of energy sources, its heat producing qualities are unique, as are its mining and production techniques. Coal is also sold at a delivered price per BTU significantly lower than other fuels, which makes it the fuel of choice for consumers—especially stream-driven electric utilities—for which fuel is the principal cost of production even in the face of small or temporary reductions in the price of other fuels such as oil or gas. Accordingly, while energy may have been a relevant product market in the instant case, coal by itself was also a relevant submarket.

The district court's error in rejecting the government's proposed geographic markets, the government argued, was the reverse of its error in rejecting the government's proposed product market. In choosing energy as the exclusive line of commerce, the trial court ignored the existence of narrower, relevant submarkets; in adopting the narrower Freight Rate Districts as geographic markets, the court ignored the existence of broader geographic markets which also constituted relevant "sections of the country" in which to analyze the effect of the combination.

Finally, the government maintained that its proof at trial made out a *prima facie* case against the combination. The government noted that the Court had found mergers *prima facie* unlawful in cases involving smaller market shares that those of Material and United Electric in either the government's proposed relevant markets, at least where, as here, concentration had been rapidly increasing. Moreover, the district court's finding that United Electric's coal reserves were inadequate to make it an effective competitor in the future was flawed, the government argued, because it rested on the same economic premise as the "failing firm" defense and must be tested against the same standard. This includes a showing that the there was no alternative to the challenged acquisition to prolonging United Electric's life, including a sale to a less anticompetitive purchaser. Here, there was no finding that United Electric's reserves were so depleted that it was about to go out of business either in 1959 or 1967 but for the acquisitions in issue, that United Electric could not have acquired additional strip reserves after 1959 or 1967, that it could not have acquired deep-mining expertise and deep mining reserves if it had not become affiliated with Material, or that Material was the only available purchaser with access to additional coal reserves.

Interestingly, although the government devoted the bulk of its brief to the market definition questions and the application of the *PNB* presumption, the defendants largely ignored these issues and focused instead on the ultimate question of whether the evidence as a whole, especially United Electric's low reserves, supported the district court's conclusion that the combination did not threaten to harm competition. In a well-placed footnote, the defendants also observed that the trial judge, Chief Judge Edwin A. Robson of the Northern District of Illinois was a distinguished antitrust jurist, having served as the coordinating judge in the civil electrical equipment cases, and was one of the principal authors of the Manual for Complex and Multidistrict Litigation.[137] The defendants also pointed out that, despite a presumably diligent search, the government was unable to find a single customer to present at trial that thought the combination had led, or was likely to lead in the future, to a substantial lessening of competition in any market.

In a five-to-four decision, the Supreme Court affirmed the dismissal of the case. Justice Potter Stewart, the author of the dissents in *Alcoa (Rome Cable)* and *Von's* who also joined Harlan's special concurrence in *Pabst*, wrote the majority opinion. Consistent with his arguments for the need of careful economic analysis to predict the competitive effect of a merger, Stewart focused on how the *PNB* presumption was both triggered *and* rebutted in the case. To this end, despite the attention paid in the government's brief to the issues of market definition, Stewart did not dwell on the question but merely accepted arguendo the government's proposed product and geographic markets and market share statistics. Stewart also readily accepted the government's view that, within these markets, the *PNB* predicates of "undue percentage share" and "a significant increase in concentration" were satisfied, thus triggering the PNB presumption of anticompetitive effect.[138]

But recalling *Brown Shoe's* caution that statistical evidence of market share and concentration, while of great significance, were not conclusive, Stewart held that it was necessary to assess the evidence of the "structure, history and probable future" of the coal industry in order to determine the applicability of the presumption and ultimately the likelihood of an anticompetitive effect from the acquisition. After

137. Brief for Appellees at 5 n.3, United States v. General Dynamics Corp., 415 U.S. 486 (1974).

138. *General Dynamics*, 415 U.S. at 494-95 nn.6-7.

embarking on a lengthy summary of the district court's findings, Stewart observed that the *PNB* presumption implicitly assumed that "a company that has maintained a certain market share in the recent past will be in a position to do so in the immediate future":[139]

> Thus, companies that have controlled sufficiently large shares of a concentrated market are barred from merger by § 7, not because of their past acts, but because their past performances imply an ability to continue to dominate with at least equal vigor. In markets involving groceries or beer, as in *Von's* and *Pabst*, statistics involving annual sales naturally indicate the power of each company to compete in the future. Evidence of the amount of annual sales is relevant as a prediction of future competitive strength, since in most markets distribution systems and brand recognition are such significant factors that one may reasonably suppose that a company which has attracted a given number of sales will retain that competitive strength.[140]

Applied to the coal industry, Stewart concluded that a company's past ability to produce, as measured by its share of industry sales, is of "limited significance" in assessing its future ability to compete. For the most past, market shares based upon sales are locked in place at any point in time, representing not contemporaneous competition on the merits but rather the obligation to fulfill previously negotiated supply contracts. Therefore, the government's reliance on market shares based on historical sales to raise an inference of likely anticompetitive effect was unjustified.

Rather, since competition manifested itself more in rivalry for new long-term contracts, which in turn necessitated an uncommitted source of coal supply, Stewart observed that a better indicator of a firm's future competitive effectiveness is its share of uncommitted reserves of recoverable coal. The record revealed that United Electric's reserve position was very weak: while it ranked fifth among Illinois producers in terms of annual production, it ranked tenth in reserve holdings with less than one percent of the reserves held by coal producers in Illinois, Indiana, and western Kentucky, having already depleted and closed many of its mines. Moreover, only about 8 percent of United Electric's reserves, representing roughly one-tenth of a percent of the three-state area industry reserves, were uncommitted. Given the weakness of United Electric as reflected in its uncommitted reserves, Stewart concluded that the district court was correct in finding that United Electric's acquisition and elimination as an independent participant in the marketplace would not substantially lessen competition.

Significantly, Stewart rejected the government's efforts to frame the analysis in terms of the "failing company" defense as the government had urged. Stewart noted that the failing company defense assumes that the challenged acquisition will lessen competition in the marketplace, but takes a "lesser of two evils" approach in permitting the transaction to go forward when the only available alternative is the failure of the company and its exit from the market. Accordingly, if the company will

139. *Id*. at 501.
140. *Id*.

not imminently fail or if other alternatives to failure are available—especially the sale of the failing firm to a less anticompetitive purchaser—the defense cannot be sustained. Stewart observed that in this case, however, the defendants did not seek to justify an anticompetitive merger, but rather sought to show that the government's statistical showing of prima facie illegality was insufficient because it did not account for the inability of United Electric to compete effectively for long-term electric utility supply contracts in the future either with its own reserves or with reserves it could obtain in the absence of the challenged combination.

Justice Douglas, joined by Justices Brennan, White and Marshall, dissented. The dissent focused on the questions of product and geographic market definition, essentially adopting the government's analysis. Since the majority predicated its *PNB* analysis on the government's proposed markets, the dissent's conclusion that the government had proved its proposed markets served to establish the prima facie case. To the dissent, then, it only remained whether the defendants had succeeded in rebutting the *prima facie* case. Douglas would have found that they did not. Douglas would have treated the rebuttal in the nature of a failing firm defense as the government had urged. The viability of a failing firm defense is judged at the time of the acquisition. But the findings of the district court as to the weakened state of United Electric's coal reserves were as of the time of trial. Although no findings were made on the state of United Electric Reserves as of 1959, the time Material first gained effective control, 21 million tons of United Electric's 52 million tons of strip reserves existing at the time of time were committed in 1968, nine years after the challenged acquisition. Likewise, the finding that there were no economically available new strip reserves was made as of the time of trial; there was no finding that new strip reserves were not available in 1959 and the record demonstrated that several other companies made new acquisitions of strip reserves in the 1960s. Finally, Douglas questioned whether United Electric could have developed, contrary to the district court's finding, expertise in deep mining to be able to tap the 27 million tons of deep mining reserves it possessed in 1959. In any event, the existence of these deep reserves may have made United Electric (or at least these deep reserves) an attractive acquisition prospect to a company with which a combination posed less of a threat to competition. Since the requisite findings to make out a failing company defense were not made, the rebuttal of the government's *prima facie* case should have failed, at least on the record so far. Douglas would have remanded the case to the district court to assess the impact of the Material-United Electric combination on the Illinois and Province markets as of 1959.

NOTES

1. General Dynamics reflects a significant generational shift in the composition of the Court. Of the five members of the majority, not a single one other than Stewart was on the Court for any of the prior antitrust merger cases. On the other hand, with the exception of Marshall—who as the Solicitor General argued vigorously to block or dissolve the mergers in *Von's* and *Pabst*—all of the dissenting justices were present for all of the Court's merger antitrust decisions in the 1960s.

United States v. General Dynamics Corp. (1974)

	President	Sworn In	Replaced
Majority			
Potter Stewart (author)	Eisenhower	Oct. 14, 1958	Harold Burton
Warren E. Burger (C.J.)	Nixon	June 23, 1969	Earl Warren
Harry Blackmun	Nixon	June 9, 1970	Abe Fortas
Lewis F. Powell	Nixon	Jan. 7, 1972	Hugo Black
William Rehnquist	Nixon	Jan. 7, 1972	John M. Harlan
Minority			
William O. Douglas (author)	Roosevelt	Apr. 17, 1939	Louis Brandeis
William J. Brennan, Jr.	Eisenhower	Oct. 16, 1956	Sherman Minton
Byron White	Kennedy	Apr. 16, 1962	Charles E. Whittaker
Thurgood Marshall	Johnson	Oct. 2, 1967	Tom C. Clark

The following chart summarizes the votes from *Philadelphia National Bank* to *General Dynamics*.

PNB* to *General Dynamics

	***PNB* (6-2)**	***Alcoa* (6-3)**		***Von's* (6-2)**	***Pabst* (9-0)**		***GD* (5-4)**
Warren	m	m		m	m	Burger	m
Black	m	m		M	M	Powell	m
Douglas	m	M		m	c		D
Clark	m	m		m	m	Marshall	d
Harlan	D	d		d	sc	Rehnquist	m
Brennan	M	m		m	m		d
Stewart	d	D		D	sc		M
White	--	m		c	sc		D
Goldberg	sc	d	Fortas	--	sc	Blackmun	m

M	Majority opinion author	D	Dissent author
m	Joined majority opinion	d	Joined dissent
c	Regular concurrence		
sc	Special concurrence		

Given their positions in *PNB*, *Alcoa*, and *Von's*, Stewart and Harlan would have been predictable votes for finding no violation in *General Dynamics*, and Rehnquist's replacement of Harlan did not affect the vote of that seat. The Burger and Powell replacements of Warren and Douglas, respectively, were critical to the Court's change of attitude toward mergers, since the votes of those seats changed. Blackmun, who replaced Fortas, provided the fifth vote. It is not clear how Fortas would have voted if he remained on the Court.

2. Since *General Dynamics* lower courts increasingly have employed more detailed and flexible qualitative analysis (albeit with varying degrees of theoretical guidance) of the likely competitive effects of proposed horizontal mergers and acquisitions. While concentration statistics continue to be the primary basis on which to predict the future competitive effects of an acquisition, plaintiffs today bear more of a burden of demonstrating the probative value of these statistics. Courts have considered a wide variety of factors in assessing the ability of the simple market structure model to predict the likelihood that the acquisition in question will be anticompetitive, including the degree of concentration and the level of sophistication among buyers; volatility in the market share distribution (particularly any trend towards deconcentration); changing demand patterns; the degree of product heterogeneity within the relevant market; the extent of excess industry capacity; the existence of vigorous competition from smaller, but strong and growing, competitors; the ease of entry into the relevant market; volatility in supplier or new customer relationships; a history of innovation from different companies in the market; the financial health of either or both of the parties, the likelihood that the acquired firm will exit the market in the absence of an acquisition; any preacquisition anticompetitive conduct by the parties; and postacquisition continuation of price competition in the market.