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Foreign Acquisitions in the United States: A Challenge to the Potential Competition Doctrine

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COMMENT

FOREIGN ACQUISITIONS IN THE UNITED STATES: A CHALLENGE TO THE POTENTIAL COMPETITION DOCTRINE

I. INTRODUCTION

The development of the law of mergers under section seven of the Clayton Act[1] has been characterized by the continuing emergence of new doctrines fashioned to plumb the depths of congressional intent on the one hand and to keep apace with a rapidly evolving national economic structure on the other. As a result of the dramatic diversification and conglomeration of American corporations in the last decade, enforcement agencies and the courts recently have struggled with the elusive principles of potential competition. Yet despite ambitious promotion of that doctrine by both the Justice Department and the FTC,[2] recent decisions of the Supreme Court[3] indicate a deep-felt judicial caution, perhaps casting a shadow of doubt on the economic coherence[4] and the legal desirability of a wholesale embrace of the twin ideas of actual potential and future potential competition.

Recent business developments, moreover, present significant new challenges to the law of mergers, challenges which may demand as extensive an expansion of legal mechanisms in this decade as the conglomerate boom summoned in the last. In the ten year period from 1963 to 1973, direct foreign capital investment in the United States mushroomed from 7.9 billion to 17.7 billion dollars.[5] Despite a present lag, such investments probably will continue. Principally as a result of the actions of corporations from sophisticated foreign economies such as those of Japan, Germany and the English speaking

1. 15 U.S.C. § 18 (1970). Section 7 provides in pertinent part: "No corporation engaged in commerce shall acquire, directly or indirectly, the whole or any part of the stock . . . or any part of the assets of another corporation engaged also in commerce, where in any line of commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly." Id.

2. See Berger & Peterson, Conglomerate Mergers and Criteria for Defining Potential Entrants, 15 Antitrust Bull. 489, 500-03 (1970) [hereinafter cited as Berger & Peterson]; Robinson, Recent Antitrust Developments: 1974, 75 Colum. L. Rev. 243, 257 (1975) [hereinafter cited as Robinson]. For a history of the Justice Department's promotion of the concept in one area, see Comment, Bank Mergers and Potential Competition, 43 Fordham L. Rev. 767 (1975).

3. United States v. Marine Bancorporation, 418 U.S. 602, 639 (1974) (refusing to reach the question reserved in United States v. Falstaff Brewing Corp., 410 U.S. 526, 537 (1973)); United States v. General Dynamics Corp., 415 U.S. 486 (1974).

4. The functional aspects of the potential competition concepts are not frequently found in reality, according to a number of commentators. See, e.g., Note, United States v. Falstaff Brewing Corporation: Potential Competition Re-examined, 72 Mich. L. Rev. 837, 848-53 (1974) [hereinafter cited as Note, Falstaff]; Comment, Toehold Acquisitions and the Potential Competition Doctrine, 40 U. Chi. L. Rev. 156, 168-71 (1972) [hereinafter cited as Comment, Toehold].

5. Elmer & Johnson, Legal Obstacles to Foreign Acquisitions of U.S. Corporations, 30 Bus. Law. 681, 682 (1975) [hereinafter cited as Elmer & Johnson]. However, during the first nine months of 1975, foreign investments in the United States declined. N.Y. Times, Oct. 27, 1975, at 4, col. 1.

nations, foreign investment in the United States now is equal to one-fifth that invested by Americans abroad.[6] Further, developing nations, demanding higher prices in return for raw materials, have begun to re-invest excess capital in more sophisticated economies. It has been estimated that the Organization of Petroleum Exporting Countries (OPEC) may gather as much as 600 billion dollars in oil revenue during the next four years alone.[7]

These developments have attracted the avid attention of the popular press, and, causing something of a "takeover paranoia," have led to a re-examination of the open door investment policy of the federal government.[8] Yet for the federal courts and the administrative agencies the problem is more immediate, because the antitrust principles of section seven must be applied now to foreign entrants. Consequently, the problematical doctrine of potential competition will be tested in yet another set of circumstances.

It is the thesis of this Comment that the current modes of legal analysis in merger cases are inadequate to deal effectively with the peculiar economic and concomitant legal aspects of foreign entry. Even without reaching broader questions of foreign policy,[9] an analysis of the transnational merger leads to the conclusion that, in at least three areas, there should be a rethinking of judicial construction of the antimerger law. These three areas include the definition of the geographic market in which the effect on competition is to be assessed, the nature and the severity of barriers to entry into that market, and the permissible modes of foreign entry into a domestic market.

Because these areas present problems which run deeply into antitrust law, and because recent Supreme Court decisions appear to signal new directions, this Comment will first analyze the fundamental elements of section seven construction. Part II will look to the definition of the product market, examining the interrelationship between product definition and actual potential competition. Part III will evaluate the geographic market, particularly the problems presented by transnational definitions. Part IV will examine barriers to entry. Here the unique economic and the collateral legal restraints placed upon the

6. Rose, The Misguided Furor About Investments from Abroad, Fortune, May 1975, at 170, 173 [hereinafter cited as Fortune].

7. Farmanfarmaian, How Can the World Afford OPEC Oil?, 53 Foreign Affairs 201 (Jan. 1975). However, one Treasury official has been quoted as saying: "From everything we have been able to learn, the OPEC investor is behaving like a nervous grandma who turns her money over to Morgan Guaranty and says: 'Here, invest it as conservatively as possible.' " Fortune, supra note 6, at 172.

8. Foreign Investors Study Act of 1974, Pub. L. No. 93-479, 88 Stat. 1450 (Oct. 26, 1974); see H.R. Res. 1296, 93d Cong., 2d Sess., 120 Cong. Rec. H8852 (1974). A spate of bills now pending in Congress would operate to restrict control and debt ownership by foreign interests. Young, The Acquisition of United States Businesses by Foreign Interests, 30 Bus. Law. 111, 112-13 (1974) [hereinafter cited as Young]. The most extreme proposal would give the President authority to veto foreign acquisitions of more than five percent of almost any publicly held corporation. Fortune, supra note 6, at 170.

9. While such questions are beyond the scope of this Comment, issues of foreign policy may, in some cases, be determinative. Most courts have been able to avoid passing on questions of policy. See, e.g., Texasgulf, Inc. v. Canada Dev. Corp., 366 F. Supp. 374, 418-19 (S.D. Tex. 1973).

foreign entrant will be discussed. Part V then will examine the modes of entry by a foreign corporation into a domestic market.

II. PRODUCT DEFINITION

In recent years the issue of relevant line of commerce increasingly has been settled by stipulation.[10] This fact, however, does not indicate necessarily that problems of product definition have been settled. Rather, when the traditional test—cross-elasticity of demand—has been argued, the issue has been hotly disputed. This has been so particularly in section two[11] monopoly cases, the classic example being *United States v. Grinnell Corp.*,[12] the most recent, the Government's action against IBM.[13] Under section seven, the most persistently difficult product definition cases have been product extension mergers.

The concept of cross-elasticity emerged from an exhaustive economic study of the flexible wrapping business in *United States v. E.I. du Pont de Nemours & Co.*[14] Rejecting the proposition that the defendant had monopolized the cellophane market, the Supreme Court found a broader "line of commerce" through a recognition that distinct but related products may compete so closely as to comprise together one product market. "This interchangeability is largely gauged by the purchase of competing products for similar uses considering the price, characteristics and adaptability of the competing commodities."[15]

Functionally, cross-elasticity operates to lessen the possible anticompetitive impact of overpricing by any single corporation. If elasticity is extremely high in a given product, the slightest price increase by one producer will lead purchasers to abandon that seller and buy elsewhere. If elasticity is low, or is offset by other competitive factors such as consumer preferences or limit-pricing, the price differential must be more significant before buyers will switch products. A series of Supreme Court cases has advanced price sensitivity as the key to cross-elasticity, and to the product market.[16]

Cross-elasticity found its way into section seven merger cases in a decision

10. See, e.g., United States v. Falstaff Brewing Corp., 410 U.S. 526, 527 (1973); United States v. Penn-Olin Chem. Co., 378 U.S. 158, 161 (1964). Particularly in gasoline cases, the market definitions have appeared "obvious" to the courts. See, e.g., United States v. Phillips Petroleum Co., 367 F. Supp. 1226 (C.D. Cal. 1973), aff'd mem., 418 U.S. 906 (1974).

11. Sherman Act § 2, 15 U.S.C.A. § 2 (Supp. 1, 1975). Section 2 provides in pertinent part: "Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony . . . ." Id.

12. 384 U.S. 563, 575 (1966).

13. United States v. IBM, Inc., Civ. No. 69-200 (S.D.N.Y., filed Jan. 17, 1969); the relevant product market is described as a "major issue" in this case. N.Y. Times, May 20, 1975, at 53, col. 8.

14. 351 U.S. 377 (1956).

15. Id. at 380-81.

16. See cases discussed in text accompanying notes 17-22 infra. On the relationship between price and cross-elasticity, see Posner, Antitrust Policy and the Supreme Court: An Analysis of the Restricted Distribution, Horizontal Merger and Potential Competition Decisions, 75 Colum. L. Rev. 282, 314 (1975) [hereinafter cited as Posner].

which had purely horizontal and purely vertical aspects, *Brown Shoe Co. v. United States.*[17] Although there the defendant proposed an extreme fractionalization of product markets, the Court had no great difficulty in applying *du Pont*—shoes are not very interchangeable. Although *Brown Shoe* characterized horizontal mergers as those involving "comparable goods or services,"[18] the cross-elasticity analysis in merger cases remained essentially uncomplicated before the emergence of the product extension acquisition. Two years after *Brown Shoe*, in *United States v. Continental Can Co.,*[19] the Supreme Court barred an acquisition of the third largest bottle producer by the second largest can manufacturer. Over the dissent of Justice Harlan, who claimed that the Court was creating a new line of commerce,[20] the decision ruled that "[w]here the area of effective competition cuts across industry lines, so must the relevant line of commerce; otherwise an adequate determination of the merger's true impact cannot be made."[21]

Finding bottles and cans to be in active competition with each other, and also finding a foreclosure of potential competition between the merging parties, *Continental Can* identified a broader product market, this time to reach a section seven violation.[22]

Similarly, in *FTC v. Procter & Gamble Co.,*[23] the Court upheld the Commissioner's finding that the purchase of Clorox, the nation's largest seller of liquid bleach, by the respondent, a detergent corporation forty times Clorox's size, violated the Clayton Act, even though the acquiring firm had never produced or sold liquid bleach. However, here the decision was not based upon a finding of a broader line of commerce encompassing the products of both firms. Instead, the Court held that the inflow of Procter's capital would serve to entrench Clorox's already dominant position in the

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17. 370 U.S. 294 (1962).

18. Id. at 334. The decision was the first authoritative post-amendment construction of the Clayton anti-merger law; Brown Shoe set forth rules as to all the fundamental elements. "The outer boundaries of a product market are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it. However, within this broad market, well-defined submarkets may exist which, in themselves, constitute product markets for antitrust purposes." Id. at 325, citing United States v. E.I. du Pont de Nemours & Co., 353 U.S. 586, 593-95 (1957) (footnote omitted).

19. 378 U.S. 441 (1964).

20. Id. at 476-77 (Harlan, J., dissenting).

21. Id. at 457. The decision was the first to dilute the careful market definitions mandated by Brown Shoe. "Where a merger is of such a size as to be inherently suspect, elaborate proof of market structure, market behavior and probable anticompetitive effects may be dispensed with in view of § 7's design to prevent undue concentration." Id. at 458 (Continental Can Co., holding 33% of the can industry, was considered already "dominant").

22. Id. at 463.

23. 386 U.S. 568 (1967). Earlier, in United States v. Penn-Olin Chem. Co., 378 U.S. 158 (1964), the Supreme Court barred a product extension joint venture, and identified actual potential competition. Id. at 174. According to a recent decision, a product extension merger under the Procter & Gamble case requires some degree of "product affinity" between the merging parties. Missouri Portland Cement Co. v. Cargill, Inc., 498 F.2d 851, 859 (2d Cir.), cert. denied, 419 U.S. 883 (1974), noted in 43 Fordham L. Rev. 484 (1974).

liquid bleach business. Unlike *Continental Can,* no new "product" was defined, but again the Court found an elimination of actual potential competition, stating that it was "clear that the existence of Procter at the edge of the industry exerted considerable influence on the market."[24]

A comparison of *Continental Can* and *Procter & Gamble* illustrates how the product extension cases appear to have minimized the importance of the cross-elasticity test in favor of the new concept of actual potential competition. The cross-elasticity test was conspicuously absent in *Procter & Gamble;* the case reached the Supreme Court escorted by a hundred page FTC decision,[25] which urged the Court to adopt the less precise analytic principles of entrenchment and potential competition.

It is not being suggested that the courts have totally abandoned cross-elasticity in favor of actual potential competition. Rather, it appears that in its haste to adopt the idea of "edge effect" and limit-pricing, the Court did not stop to consider how this new approach could be reconciled with the fundamentals of *du Pont,* and how it affects product market definition.

The most recent Supreme Court merger case in which the product line was seriously disputed was *United States v. General Dynamics Corp.*[26] In that case the district court,[27] applying *du Pont,* found sufficient cross-elasticity between coal and other forms of fuel to designate the product market as all energy products.[28] In the Supreme Court, the majority deemed this finding "superfluous" in view of the lower court's finding of no substantial lessening of competition.[29] In light of the long series of merger cases which have mandated that product and market definitions are the starting points of the analysis,[30] the *General Dynamics* Court's ability to reach a section seven decision without a product definition is, to say the least, remarkable.[31] Only the dissent saw fit to apply *du Pont,* and there Justice Douglas found the market to be coal, not energy,[32] on the basis of findings which led the judge

24. 386 U.S. 568, 581 (1967). The Court found that there was actual influence on the relevant market, that the defendant could have entered de novo, and that the defendant was the most likely potential entrant. See Pts. IV & V infra.

25. In re Procter & Gamble Co., 63 F.T.C. 1465 (1963). The FTC advanced a detailed theory of limit-pricing and its relation to barriers to entry. Id. at 1550-55.

26. 415 U.S. 486 (1974).

27. 341 F. Supp. 534 (N.D. Ill. 1972).

28. 415 U.S. at 491.

29. Id. at 510-11. The lower court relied on post-acquisition evidence to conclude that the acquired firm had lost the ability to compete effectively. See note 33 infra. One commentator has opined that the decision indicates an increased deference to the findings of district judges. Robinson, supra note 2, at 246.

30. E.g., Brown Shoe Co. v. United States, 370 U.S. 294 (1962); see cases discussed in Pt. III infra.

31. See Moyer, United States v. General Dynamics Corporation: An Interpretation, 20 Antitrust Bull. 1, 14-22 (1975) [hereinafter cited as Moyer].

32. Justice Douglas concluded that the district court's own findings demonstrated a non-elasticity between coal and other energy products, mandating a conclusion that coal was the relevant product market. 415 U.S. 486, 515 (1974) (Douglas, J., dissenting).

below to conclude the contrary, and which allowed the majority to avoid the issue altogether.

The failure to define a product market may not have been fatal to a case as unique as *General Dynamics,* which perhaps can be explained on other grounds.[33] However, the decision evidenced a disregard for the one part of the section seven test which appeared somewhat settled. Aside from the problems inherent in abandoning a competition definition of product, an error in this part of the analysis can fatally infect the geographic market definition.[34] Yet, as will be seen, that definition also suffers when the courts move away from competition definitions and toward industry definitions. Despite the warning of Justice Stewart that "the purpose of § 7 is to protect competition, not to protect competitors,"[35] the courts have continued to analyze cases in terms of competitors. As will become clear, this change in focus wreaks havoc with a transnational merger evaluation.

III. GEOGRAPHIC MARKET DEFINITION

The courts have avoided precise geographic market delineation in merger cases for a number of reasons. First, as in product definition, domestic cases have often settled the issue by stipulation.[36] Secondly, recent cases have involved true industrial giants that operate nationwide; the courts have been impressed by their pure size and have taken refuge in national market definitions.[37] Third, some cases have considered the outer lines of political subdivisions, such as state or national boundaries, to be markets, due to unique regulations those jurisdictions impose.[38] Finally, the courts have been trapped by industry delinea-

33. It has been well argued that the Dynamics Court has established a new version of the "failing company doctrine" of International Shoe Co. v. FTC, 280 U.S. 291 (1930). Robinson, supra note 2, at 250-52; see Moyer, supra note 31, at 12. This doctrine was rarely applied because its requirements were so stringent. See United States v. Diebold, Inc., 369 U.S. 654 (1962) (imminent financial collapse and unsuccessful attempts at less anticompetitive alternatives). The most extreme statement of the doctrine also required a third criterion; namely, the inability of the corporation to continue to function in receivership or through reorganization. Citizen Publishing Co. v. United States, 394 U.S. 131, 138 (1969). As to the potential impact of the Dynamics approach, see Pt. V infra.

34. This is particularly acute when the product and market definitions are closely interrelated, as perhaps they should be. See Elzinga & Hogarty, The Problem of Geographic Market Delineation in Antimerger Suits, 18 Antitrust Bull. 45, 76 (1973) [hereinafter cited as Elzinga].

35. United States v. Von's Grocery Co., 384 U.S. 270, 282 (1966) (Stewart, J., dissenting); accord, Brown Shoe Co. v. United States, 370 U.S. 294, 320 (1962) (interpreting congressional intent).

36. E.g., United States v. Falstaff Brewing Corp., 410 U.S. 526, 527 (1973); United States v. Penn-Olin Chem. Co., 378 U.S. 158 (1964). The remand in the former case illustrates that, for the government, the stipulation as to New England may have been a mistake; removal of actual potential competition of Falstaff appears to have been in the New York area. See United States v. Falstaff Brewing Corp., 383 F. Supp. 1020, 1024 (D.R.I. 1974).

37. E.g., FTC v. Procter & Gamble Co., 386 U.S. 568 (1967); United States v. Grinnell Corp., 384 U.S. 563 (1966) (monopoly case); United States v. Continental Can Co., 378 U.S. 441 (1964).

38. See text accompanying notes 67-70 infra.

tions, adopting sales territories such as states or nations for the same reason that the parties chose them in their businesses—convenience.[39]

The origins of the "section of the country test" warrant re-examination. The Supreme Court, in *Times-Picayune Publishing Co. v. United States,*[40] warned that the geographic market, "as most concepts in law or economics, cannot be measured by metes and bounds."[41] Rather, geographic market, like product market, must be delineated on the basis of a functional examination of competition. This is the rule established by *Tampa Electric Co. v. Nashville Coal Co.,*[42] in which Justice Clark wrote for the Court:

> [T]he area of effective competition in the known line of commerce must be charted by careful selection of the market area in which the seller operates, and to which the purchaser can practicably turn for supplies.[43]

The market definition of *Tampa Electric* was developed in the context of section one of the Sherman Act;[44] the *Brown Shoe* case, a post-amendment section seven Clayton Act case, adopted a similar test for the horizontal aspects of the merger.[45] Refusing to find that the relevant markets were separate urban and suburban areas, the *Brown Shoe* Court, approving a competition definition, upheld the trial judge's conclusion that effective actual competition cut across city lines.[46] Similarly, in *United States v. Philadelphia National Bank,*[47] the court employed a competition definition of geographic market, quoting *Tampa Electric* as controlling authority.[48]

39. One prominent economist has warned that the use of "selling territories" is suspect; such designations have no necessary relationship to relevant geographic markets. Elzinga, supra note 34, at 71-72.

40. 345 U.S. 594 (1953) (alleging violations of sections 1 & 2 of the Sherman Act).

41. Id. at 611. Put another way, geographic markets are not really geographic. Elzinga, supra note 34, at 47.

42. 365 U.S. 320 (1961). For an excellent discussion of the conceptual bases of the Tampa decision, see Bok, The Tampa Electric Case and the Problem of Exclusive Arrangements Under the Clayton Act [§ 3], 1961 Sup. Ct. Rev. 267.

43. 365 U.S. at 327. Professor Elzinga refers to an almost identical theory as the Marshallian conception of economic markets. "A market encompasses the primary demand and supply forces that determine a product's price and the geographic market area is the area that encompasses these buyers and sellers." Elzinga, supra note 34, at 47.

44. 15 U.S.C. § 1 (1970), as amended, 15 U.S.C.A. § 1 (Supp. 1, 1975). Tampa Electric involved the Court's review of a declaratory judgment which held illegal under section 3 of the Clayton Act, 15 U.S.C. § 14 (1970), a requirements contract between the parties. In reversing the Court of Appeals for the Sixth Circuit, the Supreme Court relied on the analyses of the leading cases interpreting section one of the Sherman Act. See 365 U.S. at 325-34.

45. "The geographic market selected must . . . both 'correspond to the commercial realities' of the industry and be economically significant." Brown Shoe Co. v. United States, 370 U.S. 294, 336-37 (1962). However, the decision's use of the term "industry" foreshadowed the shift from market to industry focus. See text accompanying notes 49-66 infra.

46. 370 U.S. at 338-39. Relying on an extensive forty-city survey, the district court came to the reasoned conclusion that the acquisition foreclosed actual competition in a series of local markets. Id.

47. 374 U.S. 321 (1963).

48. Id. at 359. The decision stated that the question of substantial lessening of competition

Regrettably, the *Tampa Electric* test did not long survive in the majority opinions of the Supreme Court. In *United States v. Grinnell Corp.*,[49] the Court in a section two Sherman Act case discounted the fact that the defendants' services were available only in a series of twenty-five mile radius areas, and ruled that:

the relevant market for determining whether the defendants have monopoly power is not the several local areas which the individual stations serve, but the broader national market that reflects the reality of the way in which they built and conduct their business.[50]

Exposition of the *Tampa* analysis was relegated to the vehement dissent of Justice Fortas.[51] In defense of *Grinnell,* it could be argued that a monopoly case properly may look more to the structure of the monopolist and less to the areas of effective competition.[52] However, in a merger case decided the same day,[53] the Court, faced with a difficult geographic market definition, effectually threw up its hands and, like *Grinnell,* adopted an industry focus rather than a market focus. *United States v. Pabst Brewing Co.*[54] barred a horizontal merger without deciding whether the geographic market comprised the single state in which the acquired corporation manufactured, the three states in which competition between the merging parties was allegedly foreclosed, or the broader national market. To the surprise of the Government, which was struggling to overcome a district court dismissal on the ground that a geographic market had not been proven,[55] the Court leapfrogged to the ultimate question. *Pabst Brewing* ruled, in effect, that to bar a horizontal merger in a concentrated industry where the number of competitors had declined, no exact geographic market need be shown.[56] It was this ruling which led Justice Harlan to accuse the majority of emasculating the phrase "in any section of the country."[57]

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must be based upon "a firm understanding of the structure of the relevant market." Yet the case also warned courts to be "alert to the danger of subverting congressional intent by permitting a too-broad economic investigation." Id. at 362.

49. 384 U.S. 563 (1966).

50. Id. at 576. In support of its definition, the Court cited the national planning of the defendants, the presence of multi-state contracts, national ratemaking and terms of contracts, and national certification by insurance issuers. Id. at 575.

51. "The central issue is where does a potential buyer look for potential suppliers of the service—what is the geographical area in which the buyer has, or, in the absence of monopoly, would have, a real choice as to price and alternative facilities?" Id. at 589 (Fortas, J., dissenting).

52. Almost by definition, a full-blown monopoly is nearly co-extensive with the relevant market which it controls. The first major monopoly case took such a focus on the defendant. See United States v. Aluminum Co. of America, 148 F.2d 416 (2d Cir. 1945) (L. Hand, J.).

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

54. Id.

55. 233 F. Supp. 475, 481 (E.D. Wis. 1964), rev'd, 384 U.S. 546 (1966).

56. 384 U.S at 549-53. Pabst relied heavily on the existence of a "trend" towards concentration. Id. at 551-53. See also United States v. Von's Grocery Co., 384 U.S. 270, 276 (1966).

57. 384 U.S. at 555 (Harlan, J., concurring). Justice Harlan, concluding that the government had indeed proven its case, concurred in the result. Id.

Although the *Pabst* decision has been severely criticized,[58] its wide-open industry focus is still favored by the Court. In *General Dynamics*, the Supreme Court appeared to employ a similar analysis, reaching a conclusion that there was no substantial lessening of competition in "any" area of the country, viz., nowhere in the industry involved.[59] This apparently relieved the Court of the necessity of passing on market definition.[60] However, in *United States v. Marine Bancorporation*,[61] the Supreme Court appeared to limit the *Pabst* approach, holding that the relevant geographic market must be co-extensive with the phrase "section of the country" and that both are equivalent to "the area in which the acquired firm is an actual, direct competitor."[62] According to one prominent commentator, the *Marine Bancorporation* decision "squarely reaffirms the necessity for delineating a realistic geographic market."[63]

This is not necessarily the case. The disintegration of the competition definition of market in merger cases has been accompanied by the emergence of the very different industry focus. If properly used, such a focus could signal a return to the basic economic philosophy of *Tampa Electric*.[64] However, it appears that instead of concentrating on lines of industry competition, this new focus looks to industry structure, thereby perhaps infringing upon the "line of commerce" inquiry, and confusing what is essentially a separate issue.[65]

Nowhere is this industry focus better illustrated than in the potential competition cases. By looking to and comparing industry structure rather than lines of supply and demand, the courts have been able to reach the elusive principles of potential competition.[66]

The bank merger cases suggest yet another approach to market definition—that of delineation by regulation. While both *Philadelphia National* and *Marine Bancorporation* appear to look to lines of supply and demand,[67] the Government in the latter case argued that entire states are

58. Professor Elzinga devoted an entire article to the task of dismembering both the government's arguments and the Court's opinion in Pabst. Upon applying an economic test fashioned to ascertain lines of supply and demand, Professor Elzinga concluded that the relevant market in Pabst was different from any of those propounded. Elzinga, supra note 34, at 50-75.

59. United States v. General Dynamics Corp., 415 U.S. 486, 510-11 (1974).

60. Id.; see Moyer, supra note 31, at 14-19.

61. 418 U.S. 602 (1974).

62. Thus the Court rejected the government's argument that, for purposes of banking, a state could be a relevant market. Id. at 620-22. See text accompanying notes 67-70 infra.

63. Robinson, supra note 2, at 258. "[A] persuasive case can be made that the present Court is faithful both to the legislative history of the statute and to the principles . . . [of] Brown Shoe." Id. at 259-60.

64. See note 43 supra and accompanying text.

65. See Elzinga, supra note 34, at 60-61.

66. In a potential competition case, instead of looking to supply and demand, the court counts competitors and judges their behavior. This approach appears to confuse the market definition with the barriers to entry analysis. See, e.g., United States v. Phillips Petroleum Co., 367 F. Supp. 1226, 1254 (C.D. Cal. 1973), aff'd mem., 418 U.S. 906 (1974).

67. See text accompanying notes 47-48 supra. In Marine Bancorporation, the Court approved a market definition which reasonably identified the area in which the "banks offer the major part

proper relevant markets, in light of the state-by-state regulation of banking.[68] This theory was rejected as inapposite to the facts of the case,[69] but the regulation definition someday may appear in a proper context. For instance, if two leading multibank holding companies in a given state were to merge, the courts would probably find a foreclosure of competition on two levels—the several local communities in which the parties compete, and the entire state in which the banks operate. The outer boundaries of the latter market would be defined because of state regulation. In addition, the casual designation of a national market in a large number of antimerger cases is in fact a regulation definition approach, based on the outer limits of the jurisdiction of the United States.[70]

Thus, it appears that the courts have considered at least three different methods of geographic market definition. These include (1) the *Tampa* test of definition by competition, which delineates markets on the basis of lines of supply and demand; (2) the *Pabst* focus on industry structure, which assesses competitive impact more broadly by looking to trends of concentration industry-wide; (3) the regulation definition, which sets the boundaries of markets because of the limits of jurisdictions. It is apparent that these tests are often combined,[71] and some are certainly more applicable to specific industries.[72] However, there is little indication that even the Supreme Court is aware of when it is using the different market tests.

While the distinction between these modes of market definition may appear elusive, in the case of a foreign entry the method employed can produce divergent results. This is well illustrated by the situation in *FTC v. British Oxygen Co.*,[73] where the district court enjoined a tender offer takeover of Airco, the second largest American gas producer, by the largest British industrial gas manufacturer (BOC). Subsequently, an FTC administrative law judge, finding significant foreclosures of actual and actual potential competition between the parties, ordered the British company to divest itself of its holdings in Airco. Further, the judge found that the acquired firm would be entrenched in the domestic market.[74] While the report of the FTC order does not expressly reveal an attempt at market definition,[75] an appli-

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of their services and to which local consumers can practicably turn for alternatives." 418 U.S. at 619.

68. "[T]he Government asserts that the State is an economically differentiated region, because its boundaries delineate an area within which Washington banks are insulated from most forms of competition by out-of-state banking organizations." Id. at 620.

69. Id. at 621-23.

70. See Elzinga, supra note 34, at 67; text accompanying notes 79-83 infra.

71. Pabst Brewing appeared to struggle with a competition definition, an industry definition and a regulation definition before abandoning the idea of defining a market. See 384 U.S. at 549-53. Arguably, every case which found a national market employed a regulation definition in tandem with at least one other test.

72. For example, the unique regulatory power of states over products such as alcohol and services such as banking or insurance could require different market tests. See note 68 supra.

73. 1974 Trade Cas. ¶ 75,003 (D. Del.).

74. British Oxygen Co., 3 Trade Reg. Rep. ¶ 20,746 (FTC 1974).

75. The opinion simply speaks in terms of a lessening of competition "in the United States." Id.

cation to this case of the tests sketched above suggests that all three were employed in the decision. For purposes of illustration, the reader is referred to the accompanying chart.

FTC v. British Oxygen Co.: The Government's Case

AIRCO, INC.	*BRITISH OXYGEN COMPANY*
(New Jersey Corporation) 1972 Sales: $492 Million	(United Kingdom Corporation) 1972 Sales: $606 Million
Market Positions: Industrial Gas (by 1972 Sales)	
1. WORLDWIDE:	
Airco: *Third Largest*; no operations outside United States	BOC: *Second Largest*; operations in nineteen nations
2. UNITED KINGDOM:	
Airco: *No Operations*	BOC: *Largest*
3. UNITED STATES:	
Airco: *Second Largest* (17% of market)	BOC: *No Operations*
Market Positions: Medical Equipment (by 1972 Sales)	
1. UNITED KINGDOM:	
Airco: *No Operations*	BOC: *Largest*
2. UNITED STATES SUBMARKETS:	
a) Inhalation Anesthetic Submarket: Airco: *Largest* (35%)	BOC: 8% (through U.S. subsidiaries)
b) Inhalation Therapy Equipment Submarket: Airco: *Second Largest* (11%)	BOC: *No Operations*
c) Medical Pipeline Systems: Airco: *Largest* (50%)	BOC: *No Operations* (except domestic paper subsidiary)

Source: FTC Application for Temporary Restraining Order and Preliminary Injunction, FTC v. British Oxygen Co., 1974 Trade Cas. ¶ 75,003 (D. Del.).

Under the *Tampa* test, it is apparent that only the aspect of foreclosure of actual competition was reached, and only in the inhalation anesthetic submarket. In that both parties were present only in that product market, that was the only market in which buyers could look to alternate means of supply. BOC's acquisition of Airco's 35 percent share, added to its own 8 percent, would certainly have entrenched Airco's leading position. However, under *Tampa*, the fact that worldwide BOC held the second market position in industrial gas would not have been at all relevant to the issue of concentration in the domestic market, because there was no showing that United States purchasers looked abroad to buy industrial gas.[76] Clearly, then, the competition definition has little place in an international potential competition case; if the buyers do not rely on the foreign entrant for products, its strong position in totally foreign markets has little or no relevance.

The industry focus in *Pabst* goes much further to explain the result in *British Oxygen*. By looking to the industry (industrial gas) rather than to the geographic market (domestic), national lines are more easily crossed and two levels of increased concentration are identified. First, the acquisition of Airco would have resulted in entrenchment; Airco would have been supported with all of BOC's resources. Further, if the "edge effect" test is applied, BOC would be eliminated as a likely entrant into the domestic industry. However, the difficulty with this approach is that the decision in the case may have been based also on a market definition which was *global,* or at least transnational. In its brief to the district court, the FTC made much of BOC's worldwide position and its dominant stance in Britain and the EEC, and raised the spectre of BOC becoming the largest in its field worldwide.[77] No consideration was given to the questions of whether and why these were relevant considerations.

There appeared to be adequate domestic market reasons to enjoin the acquisition under *Pabst*. However, the *Pabst* approach can lead a court to assess transnational concentration, without consideration of the problematic question of whether the effects doctrine goes so far as to protect foreign competitors not before the court.[78] Certainly, the transnational industry focus illustrates that the BOC acquisition would have concentrated foreign markets, but is such a consideration relevant to a domestic merger?

A regulation definition of relevant market was not apparent on the face of *British Oxygen,* but the case illustrates that in the transnational acquisition, a

76. In its brief to the district court, the FTC stated that "Airco and BOC market their inhalation anesthetic equipment and inhalation therapy equipment through distributors on a nationwide basis; Airco also markets its industrial gases and medical pipeline systems nationwide. Thus an appropriate geographic market is the United States as a whole." FTC Memorandum in Support of Application for Temporary Restraining Order and Preliminary Injunction at 26, FTC v. British Oxygen Co., 1974 Trade Cas. ¶ 75,003 (D. Del.). This statement represented the full extent of the FTC's market analysis.

77. Id. at 32. In the words of a BOC memo, the Airco acquisition " 'would create indisputably. the world no. 1 force in gas and gear-sales of 340 million pounds. . . . Not that a great many tangible economies of integration are to be achieved, rather a matter of international muscle commercially and technologically.' " Id.

78. See FTC v. Eastman Kodak Co., 274 U.S. 619 (1927) (whether the protection of foreign competitors of the defendant is within the scope of the FTC's authority). In the lower court, the decision stated, "we are of opinion that the Commission, if it deemed its action for the public interest, could promote the interests of foreign raw film makers, as has been done. The Commission's field of action is foreign as well as interstate commerce." Eastman Kodak Co. v. FTC, 7 F.2d 994, 996 (2d Cir. 1925), aff'd on other grounds, 274 U.S. 619 (1927).

finding that a national market exists no longer means that the largest market has been found. Rather, in the case of a foreign entrant, the casual designation of the United States as a relevant market appears to be a regulation definition—a jurisdictional boundary.[79] There was evidence in *British Oxygen* that BOC had both operations and further ambitions in Canada.[80] However, no consideration was given to the fact that Canada might be part of the relevant geographic market, particularly under the *Tampa* or *Pabst* approach. Although under the competition or industry definitions of market, limiting one's analysis to areas within national boundaries may not be proper, such an outer limit may be justified. The United States can impose different tariffs and taxes on foreign firms, as well as limit and regulate their operations and holdings.[81] Thus, the nation may be appropriately considered the relevant market because the transaction of business across national lines may present severe difficulties. These factors are inextricably intertwined with the barriers to entry analysis.

There may be a more fundamental reason why market definitions should stop at national lines. The language of section seven can be read to apply only to foreclosures of competition in this country;[82] concern over transnational concentration may be beyond the mandate of Congress. However, at least one court has intimated otherwise.[83]

Market definition in the case of the foreign potential entrant thus appears to be a mixture of the *Pabst* industry focus and the regulation definition. The *Tampa* test is applicable only where actual transnational competition is present. This is not the ordinary case. The problem with using *Pabst* is that courts must be very careful to distinguish between domestic and foreign industries. Further, *Pabst* is an overly vague standard, one which has been criticized as both economically faulty[84] and inconsonant with congressional intent. The problem with the regulation definition is that its ramifications have not been thoroughly considered, and it has been rejected by the one Supreme Court case in which it was offered—*Marine Bancorporation*.[85] However, the odd marriage between these two tests appears to be the only way, though perhaps an unsatisfactory one,[86] to define a market in the

79. "Jurisdictional" here does not mean the outer limits of the authority of a federal court, but rather the geographical boundaries of a nation or state.

80. FTC Memorandum in Support of Application for Temporary Restraining Order and Preliminary Injunction at 30-31, FTC v. British Oxygen Co., 1974 Trade Cas. ¶ 75,003 (D. Del.).

81. See generally Elmer & Johnson, supra note 5; Elzinga, supra note 34, at 67; Young, supra note 8. See Pt. IV infra.

82. See 15 U.S.C. § 18 (1970) ("any section of the country"); Jacobs, Acquisitions, 43 Antitrust L.J. 552, 558-59 (1975).

83. See note 78 supra.

84. See note 58 supra.

85. 418 U.S. 602, 620-22 (1974); see note 62 supra. However, the Pabst decision appeared to suggest that in light of the state power over liquor under U.S. Const. amend. XXI, Wisconsin was a separate market. See 384 U.S. 546, 560 (Harlan, J., concurring).

86. An economically rational way may not exist. Professor Posner has advised the abandonment of the potential competition doctrine, solely on the basis of the concept's domestic

transnational potential competition case. Because geographic definitions are fundamental to anti-merger decisions, this unfortunate state of affairs raises questions about the ultimate utility of the mechanism in this context.

IV. Barriers to Entry

A. *Conditions in the Target Market*

Most mergers challenged by the enforcement agencies as violative of section seven have occurred in or resulted in entries into markets characterized as oligopolies. Because oligopolies are not subject to direct attack under the antitrust laws, the Clayton Act has emerged as a tool to prevent further concentration which, it has long been presumed, is anticompetitive.[87] In *Philadelphia National Bank,* Justice Brennan, speaking for the Court, opined that the one elemental proposition accepted by economists was that a large number of competitors is desirable while a small number is anticompetitive.[88] While this position frequently has been challenged, it remains the core of the antimerger law, in that the prevention of concentration appears to be what Congress intended.[89]

With concentration as the key indicator, relevant markets have been characterized as atomized, loose oligopolies, or tight oligopolies. As the market grows more concentrated, market shares of the remaining firms rise, smaller competitors are forced out of business, and entry barriers increase. Eventually, a point is reached where the remaining firms, because of their powerful stature, begin to control some of the conditions in the market without resort to outright conspiracy reachable under the Sherman Act.[90]

experience, since "[t]here is no judicially workable method of ranking, even crudely, the potential competitors in a market . . . ." Posner, supra note 16, at 323.

87. See notes 21 & 56 supra.

88. United States v. Philadelphia Nat'l Bank, 374 U.S. 321, 363 (1963). This proposition was cited in support of the majority opinion's statement that a prima facie case of a section seven violation could be shown by (1) an "undue" percentage of market share in the post-merger firm and (2) a significant increase in concentration. Id.

89. United States v. Von's Grocery Co., 384 U.S. 270, 274-78 (1966). " 'The dominant theme pervading congressional consideration of the 1950 amendments was a fear of what was considered to be a rising tide of economic concentration in the American economy.' " Id. at 276, quoting Brown Shoe Co. v. United States, 370 U.S. 294, 315 (1962). But see United States v. Falstaff Brewing Corp., 383 F. Supp. 1020, 1022-23 (D.R.I. 1974) (no necessary relation between concentration and competition in the New England beer market; economist suggests that issues such as pricing behavior, innovation, market shares and product quality are superior indicators).

90. One of the mysteries of the potential competition doctrine is how oligopolists manage to control market conditions without price-fixing conspiracies or at least "conscious parallelism." There is a limit to the latter doctrine; see Theatre Enterprises, Inc. v. Paramount Film Distrib. Corp., 346 U.S. 537, 541 (1954) ("Circumstantial evidence of consciously parallel behavior may have made heavy inroads into the traditional judicial attitude toward conspiracy; but 'conscious parallelism' has not yet read conspiracy out of the Sherman Act entirely." (footnote omitted)). However, manufacturers' business reasons for offering their products for the same price per unit or quantity are not of themselves evidence of independent pricing sufficient to negate the inference of a conspiracy; such a result would completely frustrate enforcement of section one of the Sherman Act. See, e.g., Advertising Specialty Nat'l Ass'n v. FTC, 238 F.2d 108 (1st Cir.

Thus, when this line into oligopoly is crossed, the remaining firms can maximize profits by raising prices to reap monopoly profits, or by controlling supply to their own advantage. The net effect on the market is presumed to be similar to that caused by a full monopoly.

Mergers which result in firms obtaining dominant positions, or which "tend to create a monopoly," are violative of the Clayton Act.[91] However, the potential competition doctrine bars mergers which do none of these things. The Supreme Court has accepted the proposition that a

> merger may be unlawful if the target market is substantially concentrated, if the acquiring firm has the characteristics, capabilities, and economic incentive to render it a perceived potential *de novo* entrant, and if the acquiring firm's premerger presence on the fringe of the target market in fact tempered oligopolistic behavior on the part of existing participants in that market.[92]

This is what has been referred to as actual potential competition. The companion doctrine—future potential competition—has not been explicitly accepted by the Supreme Court.[93] That doctrine involves no edge effect; rather under that doctrine section seven encourages de novo or toehold entry, in contrast to a large acquisition, as procompetitive. The most difficult question posed by the doctrine of future potential competition is whether a present merger which is not anticompetitive can be barred because otherwise the entrant might someday enter in a theoretically more salutary fashion.[94]

Edge effect is usually expected to be evidenced by limit-pricing. *Falstaff* appeared to assume that the oligopolist will limit-price in the face of a perceived potential entrant; this assumption has been criticized as unrealistic.[95] However, the *Marine Bancorporation*[96] test does not appear to require limit-pricing per se. Instead, that opinion took refuge in a vague presumption that some sort of edge effect would occur and that the effect would temper the oligopolists' avarice.

Actual potential competition analysis operates best in the case of a geo-

1956). See generally Markham, The Nature and Significance of Price Leadership, 14 Am. Econ. Rev. 891 (1951); Turner, The Definition of Agreement Under the Sherman Act: Conscious Parallelism and Refusals to Deal, 75 Harv. L. Rev. 655, 658-66 (1962).

91. 15 U.S.C. § 18 (1970). See, e.g., FTC v. Procter & Gamble Co., 386 U.S. 568 (1967); Turner, Conglomerate Mergers and Section 7 of the Clayton Act, 78 Harv. L. Rev. 1313, 1322-23 (1965).

92. United States v. Marine Bancorporation, 418 U.S. 602, 624-25 (1974).

93. Id. at 639; accord, United States v. Falstaff Brewing Corp., 410 U.S. 526, 537 (1973).

94. "We leave for another day the question of the applicability of § 7 to a merger that will leave competition in the marketplace exactly as it was, neither hurt nor helped, and that is challengeable under § 7 only on grounds that the company could, but did not, enter de novo or through 'toe-hold' acquisition and that there is less competition than there would have been had entry been in such a manner." United States v. Falstaff Brewing Corp., 410 U.S. 526, 537 (1973) (emphasis omitted). Ten years ago Professor Turner came to the conclusion that section 7 does indeed compel the most procompetitive route. Turner, Conglomerate Mergers and Section 7 of the Clayton Act, 78 Harv. L. Rev. 1313, 1379-80 (1965).

95. Note, Falstaff, supra note 4, at 848-53.

96. See note 92 supra and accompanying text.

graphic extension merger. Whether the doctrine can operate rationally in the product extension or conglomerate situation is questionable.[97] In all cases, however, the analysis must look closely at barriers to the entrant. In the transnational case this inquiry is immensely complicated. In addition, recent Supreme Court opinions appear to recognize the operation of a wider scope of barriers, both legal and economic.[98]

B. *Legal Barriers*

In the operation of the potential competition doctrine, an acquiring party can be adjudged a probable entrant only if a barrier is not a complete bar.[99] Total legal blockades will operate completely to foreclose any entry, at least until the laws are changed. For instance, the state-by-state regulation of the banking industry usually will totally bar interstate bank mergers, at least in the case of a domestically chartered institution. However, most legal barriers are not of this extreme nature; rather, they are obstacles which can be overcome.

All acquiring firms, be they domestic or foreign, face a series of collateral federal legal obstacles to mergers. If the acquisition is effected by tender offer, the firm must satisfy the federal securities laws, which require, *inter alia,* laborious registration for the issuance of stock[100] (in the exchange offer) and notification of acquisition or intention to acquire five percent or more of the stock of any corporation.[101] In addition, the entrant will find regulations on the amount of credit he can obtain or extend in financing large stock transactions.[102] These regulations, affecting every tender offer takeover, are

97. "It would be more difficult in a product-extension merger case to determine on the basis of objective evidence alone which of several alternative courses of expansion the potential entrant was most likely to pursue." Note, Falstaff, supra note 4, at 856 (footnote omitted). The most recent case in this area resulted in a strong rebuff to the operation of potential competition in conglomerate mergers. Missouri Portland Cement Co. v. Cargill, Inc., 498 F.2d 851 (2d Cir.), cert. denied, 419 U.S. 883 (1974). However, the FTC subsequently issued a proposed complaint attacking the merger. 3 CCH Trade Reg. Rep. ¶ 20,745 (No. 741 0620, filed Oct. 31, 1974).

98. "[C]ourts must take into account the extensive federal and state regulation of banks, particularly the legal restraints on entry unique to this line of commerce." United States v. Marine Bancorporation, 418 U.S. 602, 606 (1974). "The Court lays itself open for arguments that economic, as well as legal, barriers exist for new competitors." Id. at 654 n.5 (White, J., dissenting).

99. See Note, Falstaff, supra note 4, at 846-48.

100. Securities Act of 1933 § 5, 15 U.S.C. § 77e (1970). See Wheat & Blackstone, Guideposts for a First Public Offering, 15 Bus. Law. 539, 556-58 (1960) (model registration process taking at least three months).

101. Williams Act § 14(d), 15 U.S.C. § 78n(d)(1) (1970), which makes unlawful tender offers for more than 5% of any class of equity security without specified disclosures to target shareholders and to the SEC. The Williams Act has been invoked in tandem with section 7 of the Clayton Act in a number of private cases. See, e.g., Missouri Portland Cement Co. v. Cargill, Inc., 498 F.2d 851 (2d Cir.), cert. denied, 419 U.S. 883 (1974); Texasgulf, Inc. v. Canada Dev. Corp., 366 F. Supp. 374 (S.D. Tex. 1973). On the requirements of the Williams Act generally, see Note, A Proposal for Affirmative Disclosure by Target Management During Tender Offers, 75 Colum. L. Rev. 190, 192-202 (1975).

102. Section 7 of the Securities Exchange Act of 1934, 15 U.S.C. § 78g (1970), which gives

designed to effectuate the chief objective of the securities laws: full disclosure of the character and purpose of the firm's activities.[103] While such legal restraints do not necessarily differ in varying relevant markets, their effect is different when the acquiring firm is foreign rather than domestic.

Almost all securities regulation requires detailed financial reporting of the firm's operations. False or misleading financial statements can expose the issuer to a hornet's nest of liability[104] to purchasers and investors, and can result in criminal proceedings. Certainly, for these reasons any corporation with a shaky financial or legal foundation may avoid tender offers altogether. In the case of a foreign issuer, the problems of accurate accounting are much greater; overseas accounting practices and principles vary greatly, even within the European Economic Community.[105] The foreign firm may face the significant expense of converting its entire financial reporting system to correspond with domestic systems familiar to the American investor, whom the securities laws were designed to protect. In addition, the SEC issuance and continuous disclosure reporting forms for large foreign corporations engaged in domestic stock transactions are particularly onerous.[106] Direct tender offers present a spate of additional problems for the foreign entrant, as the tortuous securities litigation in the Liquifin AG acquisition of Ronson Corporation has demonstrated.[107] Clearly, the securities regulations are more difficult for the

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the Federal Reserve Board power to regulate the credit available in exchanges for the purchase or carrying of securities. FRB Regulations T, G, U, and X (12 C.F.R. §§ 207, 220, 221, 224 (1974)) require that for certain transactions to be lawful, sufficient collateral must be presented within a specified period. See Comment, Civil Liability for Margin Violations—The Effect of Section 7(f) and Regulation X, 43 Fordham L. Rev. 93 (1974); Note, Regulation X: A Complexis, 50 Notre Dame Law. 136 (1974).

103. The announced purpose of the Securities Act of 1933 was to "provide full and fair disclosure of the character of securities sold in interstate and foreign commerce and through the mails, and to prevent frauds in the sale thereof, and for other purposes." Securities Act of 1933, ch. 38, 48 Stat. 74 (Preamble).

104. E.g., Securities Act of 1933 §§ 11-13, 15, 15 U.S.C. §§ 77k-m, 77o (1970); Feit v. Leasco Data Processing Equip. Corp., 332 F. Supp. 544 (E.D.N.Y. 1971) (Weinstein, J.). Liability in hostile tender offers can result from a myriad of problems. See, e.g., Chris-Craft Indus., Inc. v. Bangor Punta Corp., 480 F.2d 341 (2d Cir.), cert. denied, 414 U.S. 910 (1973) (violations of both Rule 10b-5 and proxy regulations).

105. Young, supra note 8, at 118. Not only the issuer, but the accountant as well may be held liable. See Hochfelder v. Ernst & Ernst, 503 F.2d 1100 (7th Cir. 1974), cert. granted, 421 U.S. 909 (1975) (applying a negligence standard).

106. Young, supra note 8, at 117. This factor alone leads foreign firms to set up domestic subsidiaries. Id. See text accompanying note 114 infra.

107. Ronson Corp. v. Liquifin AG, 483 F.2d 846 (3d Cir. 1973), remanded, 370 F. Supp. 597 (D.N.J.) (remand), aff'd, 497 F.2d 394 (3d Cir.), cert. denied, 419 U.S. 870 (1974). Additional problems are presented by SEC notification requirements contained in Sched. 13d, 17 C.F.R. § 240.13d-101 (1974). It has been held that both 13d and tender offer documents must disclose certain possible antitrust liabilities. Gulf & Western Indus., Inc. v. Great Atlantic & Pacific Tea Co., 476 F.2d 687 (2d Cir. 1973). The SEC is considering tightening these requirements. E.g., SEC Exchange Act Rel. No. 11003 (Sept. 9, 1974), [1974-1975 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 79,956. See generally Axinn, Techniques and Antitrust Aspects Concerning Foreign Entry, 43 Fordham L. Rev. 741 (1975).

foreign firm if only because domestic companies are already accustomed to operating under such laws.

These considerations and others of equal import—specifically taxes—have led to the situation where foreign firms have taken alternate routes to achieve takeovers.[108] For example, many firms will attempt to borrow huge sums of cash to buy corporations, thus avoiding the problems of stock issuance. This route is not a total solution, however; a number of the same securities laws, including the Williams Act, and proxy regulations, come into play in this situation also.[109] In addition, foreign states are concerned with cash flow, and may place their own legal obstacles in the way of a firm borrowing hundreds of millions of marks or pounds to spend in the United States. On the other hand, if the loan is obtained in this country, the foreign entrant may face complex and discriminatory regulations of the Federal Reserve Board, aimed at controlling the flow of funds to foreign interests. While recently most of these monetary restrictions have been eliminated,[110] there is no reason why new ones could not be imposed; not even an act of Congress would be necessary.

Tax problems can be significant. Not only do foreign tax laws operate to produce different and often conflicting business considerations, but international tax treaties serve to complicate the issues further.[111] For instance, a domestic firm engaged in a joint venture with a foreign entrant may desire a high percentage of voting control in order to reap the tax benefits of consolidation. Its foreign partner may similarly desire a significant voting interest in order to take advantage of its nation's laws, which encourage major participation in overseas ventures. In addition, if the foreign firm engaged in a tender offer is presently immune from federal income taxes, then that firm will lose the concomitant benefits of domestic tax deductions for the expenses incurred in the acquisition.[112] Further, the Internal Revenue Service must specifically approve acquisitions achieved by stock-for-stock reorganizations; once again, the treatment of foreign firms differs from that accorded to domestic corporations.[113]

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108. The cash tender offer has been referred to as the most frequent mode of foreign tender offers. See Young, supra note 8, at 119 n.47.

109. See note 104 supra.

110. In the 1960's major restrictions existed on stock and bond issues by foreign corporations, as well as on credit lines which banks could extend to foreign interests. These Federal Reserve Board regulations were imposed to stabilize the U.S. balance of payments. In January of 1974, President Nixon eliminated most of the restrictions, but minor regulations remain, such as the Foreign Transactions Reporting Act. See Elmer & Johnson, supra note 5, at 685-86.

111. These tax problems vary from nation to nation; the United States has entered into a series of widely differing tax treaties. Compare, e.g., Treaty with United Kingdom on Double Taxation of Income, April 16, 1945, art. III, 60 Stat. 1377, T.I.A.S. 1546, as amended, Mar. 17, 1966, [1966] 1 U.S.T. 1254, T.I.A.S. 6089, with Treaty with France on Income & Property Taxes, July 28, 1967, art. 6, [1968] 4 U.S.T. 5281, T.I.A.S. 6518. See 1 & 2 CCH Tax Treaties ¶¶ 2809 (France), 8108 (United Kingdom).

112. Young, supra note 8, at 122.

113. Before a foreign corporation can work a tax-free exchange offer, it must, in addition to meeting the requirements placed on domestic corporations, establish "to the satisfaction of the

The upshot of these collateral federal legal restraints is significant. One securities law commentator concluded that it is highly advisable for foreign firms to establish domestic subsidiaries—under the liberal corporate laws of a state such as Delaware—to serve solely as the acquisition vehicle of the parent firm.[114] Indeed, just this route was chosen by British Oxygen to facilitate its Airco acquisition.[115] The emerging prevalence of these paper companies serves to complicate the toehold analysis of a future potential competition case, as discussed in Part V.

The foreign firm also must consider the legal restraints of the several states. Presently, eleven states—including Nevada, Ohio, Virginia and Wisconsin—have special statutes regulating corporate takeovers.[116] Again, the domestic firm has the advantages of familiarity with relevant laws. At the very least, the existence of such state laws will mean more filings and greater requirements of disclosure.[117] The foreign entrant also may face archaic and discriminatory state laws which limit the amount of control which a foreign firm may exercise over a state corporation.[118] While such state laws probably are unconstitutional under the supremacy clause—because they are inconsistent with treaties[119]—or under the commerce clause—because they infringe upon Congress' plenary authority—the issues well may have to be litigated. This was the case in *Texasgulf, Inc. v. Canada Development Corp.*,[120] where the Texas firm, hostile to the takeover, raised state laws which, it argued, banned the takeover. While the Canadian corporation presented well-founded arguments as to these statutes' unconstitutionality, and the trial judge ruled the law inapplicable, the case demonstrates the existence of hidden and unexpected state legal restraints. One English practitioner has referred to such obstacles as "booby traps."[121]

Secretary or his delegate that such exchange is not in pursuance of a plan having as one of its principal purposes the avoidance of Federal income taxes." Int. Rev. Code of 1954, § 367(a).

114. Young, supra note 8, at 117. See text accompanying notes 171-74 infra.

115. See text accompanying notes 73-78 supra.

116. Workshop II: Mergers—Foreign and Domestic Take-Overs, 43 Antitrust L.J. 157, 161-62 (1975) (remarks of Mr. Robinson); N.Y. Times, Oct. 21, 1975, at 53, col. 1.

117. Young, supra note 8, at 121. State regulation can be dispositive in areas such as banking and insurance. One commentator concludes that federal and state regulation of foreign banking constitutes discrimination. Edwards, Regulation of Foreign Banking in the United States: International Reciprocity and Federal-State Conflicts, 13 Colum. J. Transnat'l L. 239, 268 (1974).

118. E.g., Tex. Rev. Civ. Stat. Ann. art. 1527 (1962), which applies to international trading corporations. "A majority of the stock shall in all instances be owned by citizens of the United States, and a majority of the officers and directors thereof shall in all instances be citizens of the United States. . . and of this State." Id. Violation can result in forfeiture of the corporate charter. The New York Business Corporation Law reveals no such restrictions. See, e.g., N.Y. Bus. Corp. Law §§ 1301, 1303 (McKinney 1963).

119. The issues presented by international treaties, particularly tax agreements, are beyond the scope of this Comment. See note 111 supra. However, as long as the state statute attempts to so regulate businesses engaged in interstate commerce, it is subject to attack under the supremacy clause, U.S. Const. art. VI, § 2. Even if interstate commerce is not involved, violations of the due process and equal protection clauses may be present.

120. 366 F. Supp. 374, 410-15 (S.D. Tex. 1973).

121. Foreign Entry into the United States—Panel Discussion, 43 Fordham L. Rev. 756 (1975) (remarks of Mr. Lever).

Beyond securities and tax laws, there are a series of federal statutes which limit certain activities to, and provide certain federal programs for, corporations substantially owned or controlled by United States' interests. Most of these are limited to specific industries, but others, such as the Overseas Private Investment Corporation (OPIC),[122] apply to any business operating abroad. Under the OPIC Act the federal government insures United States' corporations against foreign expropriation or revolution. Since participating companies must be substantially owned by United States citizens, a domestic multinational corporation may have a great advantage over a foreign multinational entrant.

In industries which bring into play considerations of national security or public policy, foreign corporations may be totally banned. While these restraints have been discussed elsewhere,[123] they include (1) defense related industries—foreign controlled firms may be barred from access to classified plans;[124] (2) maritime trade—where the lucrative "coastwise trade" is limited to firms 75% of which must be owned by Americans;[125] (3) the broadcasting and common carrier communications industry—where the FCC is prohibited by statute from granting licenses to firms under full foreign control;[126] (4) air commerce—where Civil Aeronautics Board (CAB) approval of mergers is required and where foreign control is limited to 25%;[127] and (5) atomic power—where licenses may not be issued to corporations under alien control.[128]

122. 22 U.S.C. §§ 2191 et seq. (1970). "Eligible investors" are defined as "corporations, partnerships, or other associations including nonprofit associations, created under the laws of the United States or any State or territory thereof and substantially beneficially owned by United States citizens." Id. § 2198(c)(2).

123. These federal statutes have been discussed in Elmer & Johnson, supra note 5, at 684-85.

124. See Grombach v. Oerlikon Tool & Arms Corp. of America, 276 F.2d 155 (4th Cir. 1960) (Swiss firm, manufacturing weapons in U.S. for export, was required to have security clearance; at least 75% of the stock had to be American owned).

125. The Shipping Act of 1916, 46 U.S.C. §§ 801 et seq. (1970). Section 802(a) provides in part that "in the case of a corporation, association, or partnership operating any vessel in the coastwise trade the amount of interest required to be owned by citizens of the United States shall be 75 per centum." Coastwise trade encompasses commerce between any two U.S. ports. See Central Vermont Transp. Co. v. Durning, 294 U.S. 33, 38 (1935). Passenger carriage is equally restricted; see Elmer & Johnson, supra note 5, at 689-91.

126. Communications Act of 1934, 47 U.S.C. §§ 151 et seq. (1970). Thus, for example, the FCC may not grant station licenses to, inter alia, "[a]ny corporation of which any officer or director is an alien or of which more than one-fifth of the capital stock is owned of record or voted by aliens or their representatives or by a foreign government or representative thereof, or by any corporation organized under the laws of a foreign country." Id. § 310(a)(4). The Commissioner has broad discretion to refuse to issue a license even if the requirements of the statute are met. Id. § 310(a)(5). The Act also contains a series of other restrictions on foreign participation, and all consolidations or mergers of telegraph carriers involving more than 20% foreign ownership of the resulting firm are barred; id. § 222(d). FCC approval of all other telegraph carrier mergers is required. Id. § 222(b), (c).

127. Federal Aviation Act of 1958, 49 U.S.C. §§ 1301 et seq. (1970). The CAB must approve of all mergers. Id. § 1378. Two-thirds of the directors of the corporations must be United States citizens, and 75% of voting control must be in domestic hands. Id. § 1301(13).

128. "No license may be issued to an alien or any any [sic] corporation or other entity if the

On a second level, other federal laws place conditions on foreign interests. Mineral extraction is regulated on a reciprocal basis; the United States will place the same restrictions on foreign firms as that firm's nation places on United States firms.[129] In a few areas, such as banking and oil, foreign firms can participate only if they first incorporate domestic subsidiaries for that purpose.[130] This, of course, makes the foreign interest effectively subject to suit, taxes, and regulation.

The above listings are by no means exhaustive; in regard to state laws, they are merely illustrative. Even if the restraints do not all rise to the level of antitrust considerations, the degree of foreign control may well have to be disclosed under the Williams Act.[131] A court sitting in a merger case can usually rely upon the parties to alert it to the relevant collateral legal restraints; but how these laws fit into the barriers to entry analysis has not yet been suggested.

Clearly there is no need for any extended analysis regarding the status of these laws as initial barriers. In many cases the statutes will totally bar the foreign firm; in others there are ways around the statutes.[132] Sometimes the laws prohibit only voting control; the foreign firm can thus buy a debt participation or preferred stock.[133] However, this route has two liabilities.

Commission knows or has reason to believe it is owned, controlled, or dominated by an alien, a foreign corporation, or a foreign government." Atomic Energy Act of 1954, 42 U.S.C. § 2133(d) (1970).

129. Mineral Lands Leasing Act, 30 U.S.C. § 181 et seq. (1970). Section 181 provides in part: "Citizens of another country, the laws, customs, or regulations of which deny similar or like privileges to citizens or corporations of this country, shall not by stock ownership, stock holding, or stock control, own any interest in any lease acquired under the provisions of this chapter." These provisions could cause trouble in transactions with Canada; Canada still seeks to attract foreign investment, but requires that such investment "significantly benefit" Canada. See Bergsten, Coming Investment Wars?, 53 Foreign Affairs 135 (Oct. 1974).

130. Banking, ownership of land, and drilling for oil are all possible with domestic incorporation. See Elmer & Johnson, supra note 5, at 694-97. With regard to banks, the Bank Holding Company Act of 1956, 12 U.S.C. §§ 1841 et seq. (1970), is specifically applicable. See text accompanying notes 114-15 supra.

131. See Texasgulf, Inc. v. Canada Dev. Corp., 366 F. Supp. 374, 420-31 (S.D. Tex. 1973) (violations of Clayton Act too unlikely to require disclosure, but applicable statutes restricting foreign operation must be disclosed). See notes 101 & 107 supra.

132. A business law commentator concluded that "at least for the present, neither statutes nor red tape pose significant barriers to the acquisition of control of most American corporations by foreign interests." Elmer & Johnson, supra note 5, at 698. However, the same author notes that the restrictive industry statutes place "serious limitations on the degree of day-to-day control such an alien interest could exercise." Id. at 691. De novo entry, of course, is more difficult. Presently, there appears to be a split of opinion on the extent of that difficulty. See text accompanying notes 170-74 infra.

133. Debt participation can take any number of forms, including preferred stock, bonds, and debentures. See generally H. Henn, Corporations §§ 154-56 (2d ed. 1970). With express statutory authority, common in many states, holders of debt securities may be granted voting powers; see Tracy, The Problem of Granting Voting Rights to Bondholders, 2 U. Chi. L. Rev. 208 (1935). However, even debt interests may be barred in order to stabilize the U.S. balance of payments. See 31 U.S.C. § 931 (1970) (President charged by Congress with the responsibility to "undertake

First, the foreign entrant will not achieve its goal of acquisition and control; instead, it must remain a silent partner. Second, most of the statutes are vaguely worded. It is unclear whether control alone is barred, or whether significant interests are also prohibited.[134] Since many of these statutes have not been construed, again the foreign firm may have to face litigation.

A more troublesome question is how these laws will operate as indirect barriers, specifically to restrain diversification of the foreign firm once it has entered the market. For instance, a foreign entrant may be able to enter the domestic oil market merely by domestic incorporation. But if the oligopolists in the domestic oil industry plan diversifications into atomic energy, the foreigner effectively may be barred from such ventures. Or, if the oil firms desire forward integration, and thus build and operate tanker fleets,[135] domestic rivals will have significant advantages, both in subsidizing construction and in coastline trade. The continuing trend towards diversification across industry lines demonstrates that the foreign interest may be placed at a serious competitive disadvantage. While the courts have not yet considered diversification potential as part of the barriers to entry analysis, *Marine Bancorporation* indicated that in unique industries the Supreme Court will look more closely at how the putative entrant would fare in the market.[136]

This assessment of legal barriers should not ignore the fact that a foreign entrant may gain legal benefits from its transnational stance during the takeover. Because the firm is located elsewhere, it need only insure that its domestic operations comply with domestic laws. As noted above, foreign firms are, to a great extent, exempt from federal income taxes. In addition, the policy position of the enforcement agencies still is to encourage foreign investment.[137]

continuous surveillance over the private flow of dollar funds from the United States to foreign countries . . . ."). See note 110 supra and accompanying text.

134. Most of the statutes discussed refer to "stock" and thus to voting control; however, a number speak in terms of "interest" which arguably could include debt participation. See notes 124-29 supra; Elmer & Johnson, supra note 5, at 684-85.

135. This is what the OPEC states have been doing; however, OPEC has been buying rather than assembling tankers. See Robards, The Oil Powers Assemble a Tanker Fleet, N.Y. Times, March 23, 1975, § 3 (Business and Finance) at 1, col. 1.

136. Referring in his dissent to the majority opinion, Justice White stated that the decision "erects formidable barriers to the application of the potential-competition doctrine not only in the banking business but in other lines of commerce. . . . The courts must also examine conditions in the market and conclude for themselves that there is a realistic expectation that the new entrant will appropriate for itself a substantial part of the business of the major competitors in the market." United States v. Marine Bancorporation, 418 U.S. 602, 654 (1974) (White, J., dissenting). "[T]here are unmistakable signs that the Court's general approach to section 7 is undergoing a significant transformation." Robinson, supra note 2, at 246.

137. At present, the position of the Justice Department is to give equal treatment to foreign and domestic mergers. Address by K.I. Clearwaters, Special Ass't to the Ass't Attorney General in charge of the Antitrust Division, to the Ass'n of General Counsel, May 4, 1973, in 5 CCH Trade Reg. Rep. ¶ 50,169, at 55,302-03 (1973). The official position as regards foreign entry was recently restated by Mr. Davidow, Chief, Foreign Commerce Section: "I think we certainly intend, for the foreseeable future, to continue to view any demands for anti-foreign enforcement,

The *Texasgulf*[138] decision illustrated many of these advantages. In that case a domestic minerals firm failed to obtain an injunction to halt a lightning cash tender offer takeover by the Canada Development Corporation (CDC). CDC was chartered by the Canadian Government, *inter alia*, to acquire companies engaged in the exploitation of Canadian resources. The announced goal was to preserve the benefits of Canadian resources for Canadian citizens.[139] CDC thus operated as a closed-end investment trust. In the case of the Texasgulf takeover, CDC was able to obtain a 235 million dollar credit line from its government and from Canadian banks.[140] In the United States District Court, Texasgulf charged that, in order to keep down the price at which it could acquire control, CDC conspired to violate the Williams Act. In fact, CDC did conceal the early participation of a private Canadian firm, Noranda Mines, in the first stages of the takeover. Noranda itself held shares of Texasgulf and acted as agent for CDC in the initial stock purchases. Further, even after Noranda pulled out of the contemplated joint acquisition, it attempted to obtain a shareholder list of Texasgulf. Brushing aside evidence of a series of interactions between CDC and Noranda regarding Texasgulf, the district court held that Texasgulf was not entitled to an injunction because it had failed to prove a conspiracy. Further, the court concluded that the CDC tender offer and 13d schedule were "lawful when made;" neither the offer nor the schedule made *any* mention of Noranda's participation.[141]

The proposition that emerged was that a foreign interest—particularly a foreign public interest such as CDC—can tailor its United States activities to United States law while apparently engaging in acts overseas which it could not do in the United States with equal impunity. Significantly the refusal of the court in *Texasgulf* to enjoin the takeover was not for want of jurisdiction, but rather, was due to a failure of the court to scrutinize closely the events which took place in the offices of the Canadian concerns. Considering that takeovers are often campaigns on many fronts, this partial immunity for acts outside the United States can be a distinct advantage for the foreign entrant.

Texasgulf also raises the thorny issue of a foreign state as entrant. While CDC is not exactly the alter ego of the Canadian government, it did operate to achieve a specific governmental policy. Foreign states have never been subject to United States antitrust laws, since they are immunized by the act of state doctrine.[142] Foreign states must comply with the securities laws if

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or legislation, with a very critical eye." Foreign Entry into the United States—Panel Discussion, 43 Fordham L. Rev. 756, 758 (1975) (remarks of Mr. Davidow).

138. 366 F. Supp. 374 (S.D. Tex. 1973).

139. Id. at 383-84.

140. CDC, a government corporation which will sell 90% of its shares to Canadians at some future date, obtained 75 million dollars from the Canadian Government and 160 million from Canadian banking institutions. Id. at 383, 400. CDC is presently engaged in preparing its first public issue to Canadian citizens. See Toronto Globe and Mail, July 30, 1975 at B5, col. 5.

141. 366 F. Supp. at 391-95, 397-400, 431-32; see notes 101 and 107 supra.

142. The act of state doctrine has been excluded from consideration in this Comment in that the cases and examples discussed, with the exception of Texasgulf, involve private parties. With regard to the problems presented by the doctrine, see generally Fugate, Antitrust Jurisdiction and

they are to sell stock here,[143] and there is no doubt that it was within the power of the district court to enjoin the CDC tender offer. Because of the result in *Texasgulf*, the court was not faced with the more difficult question of whether a federal judge can order a foreign state to divest a domestic acquisition.[144]

C. *Economic Barriers*

One commentator has suggested that there are in fact two types of economic barriers to entry, time-lag barriers and "true" economic barriers.[145] This distinction is useful in evaluating the situation of the foreign entrant.

Time barriers assess the period during which the entrant may face significant losses or be compelled to make alternate arrangements before its facilities in the new market are fully operational.[146] Thus, if an oil company undertakes a de novo market extension to achieve full national status, it may, for example, purchase a distribution system and crude oil reserves. However, to fully enter a new gasoline market, the entrant will have to wait a period of up to five years before refinery construction is completed. During that five years the new competitor must keep the distribution system going, and will desire to switch over to nationwide advertising, with its attendant economies of scale. Because a significant period of time must pass before the firm can sell its own refined gas, the entrant must find a supply of exchange gas and swap its crude oil for finished product until plants are complete. This de novo scenario[147] is comparable to those which exist in many other vertically integrated industries.

The mergers described in *United States v. Phillips Petroleum Co.* and *Falstaff* were undertaken so that the entrant could take advantage of, *inter alia*, the economies of national advertising.[148] In each case the defendant was "going national" by entering one significant market in which it previously had

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Foreign Sovereignty, 49 Va. L. Rev. 925 (1963); Reeves, The Foreign Sovereign Before United States Courts, 38 Fordham L. Rev. 455 (1970).

143. 15 U.S.C. §§ 77b(2), 77g (1970); see SEC v. Chinese Consol. Benev. Ass'n, 120 F.2d 738 (2d Cir. 1941). With regard to the application of the anti-fraud provisions of the Securities Exchange Act to foreign private issuers, see Bersch v. Drexel Firestone, 519 F.2d 974 (2d Cir., 1975); Leasco Data Processing Equip. Corp. v. Maxwell, 468 F.2d 1326 (2d Cir. 1972).

144. Although the court found no antitrust violations, CDC offered to be enjoined from any such violations, and the court did so. 366 F. Supp. 374, 431 (S.D. Tex. 1973). Under the final settlement CDC obtained 30% of Texasgulf and one-third membership on the board of directors. Elmer & Johnson, supra note 5, at 681.

145. Comment, Toehold, supra note 4, at 168.

146. Id. at 168-69. The longer the time-lag for entry, the more likely the oligopolists will raise prices to make short-run profits, settling for a smaller share of the market when the de novo entrant arrives. Id.

147. See United States v. Phillips Petroleum Co., 367 F. Supp. 1226, 1248-51 (C.D. Cal. 1973), aff'd mem., 418 U.S. 906 (1974) (describing the de novo expansion of comparable firms to conclude that defendant should have done likewise).

148. Id. at 1245-46; United States v. Falstaff Brewing Corp., 410 U.S. 526, 529 (1973). The Supreme Court has always paid great attention to the power and economies of advertising in consumer goods merger cases. See, e.g., FTC v. Procter & Gamble Co., 386 U.S. 568, 575 (1967).

not operated. An advantage such as this may offset high entry barriers; a domestic giant can trade on its near-national reputation to muscle its way into the new market.[149] However, no such advantage will accrue to a foreign entrant, unless that competitor enjoys an *international* reputation. In addition, because the U.S. market is highly sophisticated competitively, foreign firms have moved more slowly, testing the waters in various submarkets before deciding to move in on a large scale. This was the plan of action of British Oxygen Co., which set up a series of domestic subsidiaries before attempting its takeover of Airco.[150] These economic realities, aggravated by pure distance as well as by varying cultural and purchasing patterns in the foreign and the domestic spheres, must not be ignored. Courts should recognize that it may be much more difficult for a foreign entrant to overcome the economic disadvantages of time barriers; and that, in order to enter, the foreign firm must follow a different pattern of behavior.

"True" economic barriers are those actual costs which the entrant, but not the oligopolists in the market, must incur.[151] Here too the barriers are higher for a foreign firm. Market extension mergers are often motivated by the presence of excess production.[152] That excess can help a new competitor in overcoming the difficulties of transition. Clearly, it is much easier to ship excess goods across state lines than it is to ship from overseas. Many imports face special tariffs.[153] In addition, the federal anti-dumping laws recently have been toughened; these laws prevent a foreign firm from selling its products in the United States at prices lower than those at which it sells its products domestically.[154] Because of these discriminatory laws, a foreign manufacturer which is expanding into the United States still probably would dispose of excess production somewhere closer to home. In this area, it is apparent that a Canadian firm may be able to sell excess production in the United States, but a British firm is more likely to dispose of excess within the Common Market.

One economic study has concluded that product extension mergers are often motivated by the threat of unused resources.[155] Here the domestic rival has a prime advantage over the foreign entrant for similar reasons as those just noted. Clearly, vertical integration, forward or reverse, is more easily achieved within one nation than it is transnationally. Some of the factors involved are purely the result of accidents of history and geography. The United States is relatively isolated from other sophisticated nations (excepting Canada) by the Atlantic and the Pacific. Most nearby nations—those in

149. See Note, Falstaff, supra note 4, at 847.

150. See notes 172-74 infra and accompanying text.

151. Comment, Toehold, supra note 4, at 168.

152. Cf. United States v. Falstaff Brewing Corp., 383 F. Supp. 1020, 1024 (D.R.I. 1974).

153. E.g., President Ford's special import fee on foreign crude oil. N.Y. Times, May 22, 1975, at 1, col. 2; see Elzinga, supra note 34, at 67.

154. Anti-Dumping Act of 1921, 19 U.S.C.A. §§ 160-71 (Supp. 1, 1975), amending 19 U.S.C. §§ 160-71 (1970). See Fortune, supra note 6, at 175.

155. Hale & Hale, Potential Competition Under Section 7: The Supreme Court's Crystal Ball, 1964 Sup. Ct. Rev. 171, 183 (citing a study by Professor Chandler).

Central and South America—are underdeveloped and thus are not likely sources of highpowered competitors.[156]

Beyond these readily apparent disparities between transnational and domestic mergers are the vaguer but equally significant problems of consumer recognition, managerial skill and risk aversion.[157] A foreign firm's decision to enter the United States is a significant one; many firms simply do not have the expertise to break into some of the most sophisticated oligopolies in the world. In this light the fear of OPEC petrodollars fades; OPEC may vertically integrate its oil business, but the prospect of any of these countries controlling and managing domestic firms in unrelated industries is less likely.[158] Instead, the OPEC states will probably purchase debt interests, and be content to reap the profits of American efforts.

In other contexts, foreign firms may be unable to withstand the heat of competition. Thus, in the *Calnetics Corp. v. Volkswagen of America, Inc.*,[159] Volkswagen bought Delanair from an English firm, which wanted to get out of the American automobile airconditioner market not because it was declining but because it was mushrooming.[160] Clearly the foreign firm doubted its own ability to keep pace with domestic rivals. In consumer goods industries, a lack of customer recognition can seriously hamper a foreign entrant. Few Americans, for instance, are aware of the name "Evian," which is almost synonymous with its product—bottled water—in France. If Evian and Deer Park Mountain Spring were rivals moving into a new domestic market where neither previously had operated, Deer Park would have both the advantages of consumer recognition and of the significant advertising economies of scale. Further, even if Americans knew of Evian, prejudices or ethnocentric attitudes arguably may affect purchasing patterns.

Finally, the decision of the entrant to move into the United States market will depend upon its own assessment of how its presence will affect conditions there and whether it can make a sufficient profit. It is clear that many foreign businessmen feel ill-equipped to foray into the American economy, for both business and cultural reasons.[161] Whether entry is in truth as difficult as

156. On the relative unimportance of developing nations in the transnation strategy of multinationals, see Drucker, Multinationals and Developing Countries: Myths and Realities, 53 Foreign Affairs 121 (Oct. 1974).

157. Risk aversion constitutes the degree to which the acquiring firm will be able to withstand significant economic losses in the initial post-entry period. For example, Phillips was able to absorb a 100 million dollar loss following its takeover of Tidewater Oil. See United States v. Phillips Petroleum, 367 F. Supp. 1226, 1241 (C.D. Cal. 1973), aff'd mem., 418 U.S. 906 (1974). On the need for managerial skill, see Texasgulf, Inc. v. Canada Dev. Corp., 366 F. Supp. 374, 408 (S.D. Tex. 1973).

158. Fortune, supra note 6, at 172.

159. 348 F. Supp. 606 (C.D. Cal. 1972).

160. In 1968-69, the U.S. market for quality car airconditioners experienced rapid expansion. The English firm desired to avoid large-scale participation in American manufacturing. Id. at 612.

161. "I think it would be illusory . . . for you to suppose that a lot of foreign businessmen are going to fall over themselves to start from scratch in this country. Therefore, they may not be the potential competitors that you perceive them to be unless they are allowed to make some

believed, the fact that foreigners feel apprehensive about entry is relevant, since the potential competition doctrine deals with perceptions.

D. *Barriers to Entry: The Uses of Precedent*

In the previous sections, obstacles to entry have been discussed in their broadest scope. However, for the practitioner, it is important to consider the extent to which the precedent of domestic cases will be controlling in a challenge to foreign entry. Although there have been few cases which have reached a section seven violation solely on grounds of potential competition,[162] those cases do tend to concentrate the analysis in certain areas.

In assessing barriers, the *Falstaff* decision in the Supreme Court compared the defendant to its rival competitors, reviewing the history of market shares, the number of other potential entrants, their geographic location (i.e., how many were not presently in the relevant market), and the national size of the defendant and its actual competitors.[163] *Phillips Petroleum* considered all these factors, as well as the expansion history of rivals, in order to discover the "most likely" potential entrant, in terms of financial and managerial capabilities.[164]

It is difficult to see how this comparative analysis can be transplanted intact into the foreign case. By definition, a foreign entrant does not have a national size by United States standards; its stature cannot easily be compared to that of American companies. Courts in foreign acquisition cases will be less able to rely upon rank: the largest Dutch competitor considered may be insignificant compared to an American rival ranked 25th here, unless the Dutch firm happens to be Royal Dutch/Shell. It may well be an exercise in futility to attempt to "rank" a foreign comglomerate such as the Unilever Group next to American firms. In assessing barriers, then, federal courts will be forced to abandon the familiar and convenient yardsticks of rank and market shares and instead look more closely to pure size; *i.e.*, to factors such as assets, gross sales, debt/equity ratios, etc. It can be expected that the inapplicability of traditional tests[165] will force courts to delve deeply into the character of the

take-over." Foreign Entry into the United States—Panel Discussion, 43 Fordham L. Rev. 756, 757 (1975) (Remarks of Mr. Lever); see Jacobs, Acquisitions, 43 Anti. L.J. 552 (1975).

162. United States v. Phillips Petroleum Co., 367 F. Supp. 1226 (C.D. Cal. 1973), aff'd mem., 418 U.S. 906 (1974), is, in fact, the only case to reach final judgment on this ground. United States v. Falstaff Brewing Corp., 410 U.S. 526 (1973), remanded the decision to assess the issue of potential competition, but the district court on remand found no violation. United States v. Falstaff Brewing Corp., 383 F. Supp. 1020 (D.R.I. 1974).

163. 410 U.S. at 527-29.

164. The Phillips decision engaged in a remarkably thorough comparison between the defendant oil company and its various rivals, assessing past history of expansion, asset levels, debt/equity ratios, growth rates and profits, as well as national and international stature and diversification potential of the defendant. 367 F. Supp. at 1229, 1240, 1246-55.

165. E.g., Brown Shoe Co. v. United States, 370 U.S. 294, 328-34 (1962) (test for domestic companies). "Specifically, we think that a merger which produces a firm controlling an undue percentage share 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

firms involved, pursuing complex business analyses in all but the most obvious cases. It will be to the advantage of a foreign defendant to point out that its rank in its home nation is not necessarily comparable to ranks in the United States, that its competitors and other potential entrants may be spread all over the globe, and that meaningful comparisons to find the "most likely" foreign entrant are immensely complicated.

It is also to the advantage of the foreign defendant that the Supreme Court has refused to adopt the idea of future potential competition[166] and that the Court has consistently required actual evidence of "edge effect" in present potential cases.[167] As the previous discussion has indicated,[168] "edge effect" is certainly less likely to be found in the transnational case, in light of the fact that excess foreign production cannot easily be utilized; foreign entrants cannot trade on existing consumer recognition to "go national" and, most essentially, in most areas purchasers of goods and services simply do not "go window shopping" on an international scale.

If no transnational edge effect is found, the courts should hesitate to switch to the toehold analysis, which is properly part of only future potential cases;[169] and the concept has not been accepted in domestic situations by any means. In the foreign context, it is vital to distinguish entry into a market by small acquisition (toehold) from entry into a country by small incorporation.

It has been intimated by some practitioners that larger toeholds should be afforded the foreign entrant.[170] There is support for this position in the significant evidence, much of it discussed above, that the unique barriers facing a foreign firm militate against de novo entry in most cases. However, it is here suggested that the foreign firm needs not a larger toehold but "toeholds" in different situations. Foreign firms should be allowed to maintain perhaps two or more toeholds, as did British Oxygen,[171] without being

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be enjoined in the absence of evidence clearly showing that the merger is not likely to have such anticompetitive effects. . . . Such a test lightens the burden of proving illegality . . . ." United States v. Philadelphia Nat'l Bank, 374 U.S. 321, 363 (1963) (citation omitted).

166. See notes 2-4 supra and accompanying text.

167. See note 92 supra and accompanying text.

168. See Pt. IV(A) & (B) supra.

169. Comment, Toehold, supra note 4, at 177. The FTC first adopted the toehold concept in Bendix Corp., [1970-73 Transfer Binder] Trade Reg. Rep. ¶ 19,288, at 21,445 (FTC 1970), vacated and remanded, 450 F.2d 534 (6th Cir. 1971) (remanded because toehold theory was not presented during administrative hearing or discussed by complaint counsel in the appeal to the Commission). In a number of cases, the FTC has in effect created a presumption that if the entrant could make a large acquisition, a fortiori it could, and should, enter by toehold. Comment, Toehold, supra note 4, at 175-76. The Supreme Court has twice avoided passing on the concept by equating toehold with de novo entry. United States v. Falstaff Brewing Corp., 410 U.S. 526, 530 n.10 (1973); accord, United States v. Marine Bancorporation, 418 U.S. 602, 625, 632 (1974). Other courts have also sought to avoid the theory. See, e.g., Stanley Works v. FTC, 469 F.2d 498, 508 n.24 (2d Cir. 1972), cert. denied, 412 U.S. 928 (1973) (refusing to adopt FTC's potential competition analysis but barring a merger upon a finding of foreclosure of actual competition).

170. See note 161 supra.

171. FTC Application for Temporary Restraining Order and Preliminary Injunction at 13-14, FTC v. British Oxygen Co., 1974 Trade Cas. ¶ 75,003 (D. Del.).

regarded as having embarked on a predatory campaign. Further, when the merger is a transnational market extension, toeholds should be allowed where there is an absence of proof of actual perception (edge effect) by the oligopolists. These recommendations are based upon the conclusion that the foreign entrant does not merely have a more difficult time of it, but rather that its behavior *must* be different.

The best illustration of this difference is the interrelation of the toehold concept with the prevalence of the domestic subsidiary acquisition vehicle. British Oxygen Co. set up two such firms in the United States, one to acquire Airco and a second to acquire and consolidate its present domestic holdings.[172] In the proceedings, both the court and the FTC appeared to lose sight of the fact that these acquisition vehicles are little more than ephemeral corporate entities. When a corporation is to be used solely as an acquisition vehicle, little more than a bank account is required.[173] The foreign firm merely incorporates the holding company, guarantees its loans, and the company can begin acquiring domestic firms.[174] However, the FTC and the courts appeared to be regarding the existence of these acquisition vehicles as evidence of de novo intentions, or worse, as evidence of part of a predatory plan of multiple acquisition. As a result, foreign firms may be penalized for not turning these tiny companies into functioning operations.

V. CONCLUSION

Foreign firms desiring to acquire domestic companies are at a unique disadvantage. For many reasons, a United States firm of comparable stature is more likely to succeed in any plan of expansion into a new American market. Foreign entrants face myriad legal obstacles to mergers. In regard to those which apply to all mergers, foreigners are disadvantaged because of their lack of familiarity with securities laws, monetary regulations, and state laws, as well as with the antitrust laws themselves.[175] Further, numerous federal statutes operate to bar or hinder foreign entry in a fashion which is discriminatory.

Financially, foreign companies must deal with significant economic problems not encountered by domestic corporations. These problems include disutility of excess production and unused resources, the unavailability of advertising economies, and the absence of consumer recognition. Not only are the barriers to foreign entry higher than those to domestic expansion, but also the nature of the barriers differs widely.

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172. Id. at 3.

173. "BOC Financial [the acquisition vehicle] is merely the alter ego of BOC, organized solely for the purpose of the tender offer for the shares of Airco . . . ." Id. at 8.

174. See Young, supra note 8, at 117.

175. See Pt. IV(B) supra. The impact of the threat of antitrust action must not be minimized. In a recent case, a simple letter by the Justice Department announcing intention to file suit halted an acquisition of Miller Printing Machinery Co. by Gutehoffnungshutte Aktienverein of West Germany two days before the takeover was scheduled. Both firms had previously operated solely in their own countries. The takeover was postponed "indefinitely." See BNA Antitrust & Trade Reg. Rep. No. 718, at A-30 (June 17, 1975).

It has been shown that the transaction of business—as well as the achievement of mergers—across national lines is difficult. It is suggested that the recognition of this difficulty presents a solution to the unresolved problems of geographic market definition.[176] For both legal and economic reasons, the choice of this nation as a whole as the relevant market appears justifiable. In this regard the courts have been reaching a proper result, albeit thus far unaided by any rationale.[177] However, if in any case there is evidence of a transnational edge effect or international buying and selling of the relevant product on a large scale, courts will still have to consider whether a larger or a different market in fact exists.

In reviewing the nature and conduct of a foreign firm, courts must recognize the difficulties of comparison analysis.[178] Industry ranks and market shares cannot be employed with the same confidence as in the past. The potential entrant analysis must be more thorough and more penetrating. Of all the potential competition cases, only *Phillips Petroleum*[179] stands out as an analysis sufficiently penetrating to serve as a model for a foreign acquisition case. By contrast, the decisions in *British Oxygen*[180] and *Texasgulf*[181] are quite inadequate.

If the enforcement agencies and courts desire only to halt or interfere with foreign acquisitions in this nation, then the current casual application of the potential competition doctrine will achieve that discriminatory result. However, if the Clayton Act is to be fairly applied, the courts must distinguish foreign cases from domestic cases, and present modes of judicial analysis must be modified and supplemented.

*Howard R. Hawkins, Jr.**

176. See Pt. III supra.

177. See text accompanying notes 71-72 supra.

178. See text accompanying note 165 supra.

179. United States v. Phillips Petroleum Co., 367 F. Supp. 1226 (C.D. Cal. 1973), aff'd mem., 418 U.S. 906 (1974), discussed in text accompanying note 164 supra.

180. FTC v. British Oxygen Co., 1974 Trade Cas. ¶ 75,003 (D. Del.) (injunction); British Oxygen Co., 3 Trade Reg. Rep. ¶ 20,746 (FTC 1974) (divestiture).

181. Texasgulf, Inc. v. Canada Dev. Corp., 366 F. Supp. 374 (S.D. Tex. 1973).

* The author was Writing and Research Editor of Volume 43 of the *Fordham Law Review*.