



1969

Restraint of New Enterprise Joint Ventures as a Matter of Unreasonable Probability

Frank L. McClendon Jr.

Follow this and additional works at: <https://scholar.smu.edu/smulr>

Recommended Citation

Frank L. McClendon Jr., *Restraint of New Enterprise Joint Ventures as a Matter of Unreasonable Probability*, 23 Sw L.J. 299 (1969)
<https://scholar.smu.edu/smulr/vol23/iss2/3>

This Article is brought to you for free and open access by the Law Journals at SMU Scholar. It has been accepted for inclusion in SMU Law Review by an authorized administrator of SMU Scholar. For more information, please visit <http://digitalrepository.smu.edu>.

RESTRAINT OF NEW ENTERPRISE JOINT VENTURES AS A MATTER OF UNREASONABLE PROBABILITY

by

Frank L. McClendon, Jr.*

JOINT ventures, as a form of business association for sharing risks and profits, have long been known to commerce¹ but only recently given a distinctive recognition in law.² In terms of economic impact the phenomenon is even more recent. Use of joint ventures as a business device has increased from a small base to enormous proportions in the post-World War II era. Use of the device as a convenient means to provide the great concentrations of economic resources, knowledge, and skill necessary to meet many modern day business situations has led to this rise to prominence and wide utilization.³

The many combinations that may be involved in joint activity,⁴ and the many applications thereof, have led inevitably to antitrust scrutiny. Recent governmental attacks on the joint venture as a legal entity within the purview of antitrust laws have stimulated much controversy and speculation.⁵ Although the courts now have provided some guidance, commentators are divided as to the proper approach which should be adopted in evaluating the antitrust legality of joint venture relationships. The purpose of this Article is to analyze the impact of antitrust laws, especially the Sherman Act⁶ and section 7 of the Clayton Act,⁷ on corporate new business joint activity and to offer suggestions for coping with the problems presented.⁸

* B.S., University of Texas; LL.B., University of Texas; LL.M., Southern Methodist University. Attorney at Law, Los Angeles, California.

¹ S. WILLISTON, A TREATISE ON THE LAW OF CONTRACTS §§ 318-318C (3d ed. 1959).

² "The concept of joint adventure as a legal relationship or association *sui generis* is purely of American origin dating from about 1890. Just how or why it originated no one seems precisely to know." State *ex rel.* Crane Co. v. Stokke, 65 S.D. 207, 272 N.W. 811, 817 (1937).

³ Tractenberg, *Joint Ventures on the Domestic Front: A Study in Uncertainty*, 8 ANTITRUST BULL. 797 (1963).

⁴ "Examples of parties associating themselves in joint ventures, in addition to individual persons, include syndicates and partnerships, partnerships and partnerships, individual persons and partnerships, individual persons and corporations, corporations with other corporations, corporations with joint ventures and corporations with partnerships, limited or otherwise." S. WILLISTON, *supra* note 1, § 318C, at 620-21.

⁵ "The current interest of the Antitrust Division in joint ventures well illustrates the ambivalent and constantly changing emphasis of antitrust enforcement policy." Gesell, *Joint Ventures in the Light of Recent Antitrust Developments: Joint Ventures and the Prosecutor*, 10 ANTITRUST BULL. 31 (1965).

⁶ Sherman Act, 15 U.S.C. §§ 1, 2 (1964).

⁷ 15 U.S.C. § 18 (1964), formerly 38 Stat. 731 (1914).

⁸ Section 5(a) of the Federal Trade Commission Act, 15 U.S.C. § 45(a) (1964), will be excluded from consideration herein. It must be noted, however, that in the future the Commission may seek to further augment its all-encompassing banner of "unfair methods of competition in commerce," and lay siege on joint ventures. This has been strongly hinted by Chairman Dixon, who stated: "To function effectively the Commission must do more than merely challenge old practices. It must also observe and evaluate new ones which may be developing so that, if necessary, prompt action may be taken against them. These new practices may include some old ones which sometimes reappear in their original guise but often in a somewhat different one, as is now the case with respect to joint ventures."

Chairman Dixon's speech singled out "vast corporate estates" of joint ventures in the glass, chemical, petro-chemical and steel industries which mostly involved actual competitors in the same

I. THE JOINT VENTURE CONCEPT

Definitional Problems. Basic to a meaningful discussion is the problem of delineating those types of joint business activities which are more likely to be sensitive to antitrust challenges. The most significant problems have emerged when two or more corporations associate for a business purpose. The combination activities may include simple agreements for joint research, resource development, bidding, buying, or selling, or may involve more sophisticated agreements creating a joint subsidiary. Of the two degrees of joint corporate activity, the jointly owned and incorporated subsidiary currently presents the greater challenge and will be exclusively dealt with herein. With respect to joint subsidiaries, the emphasis herein shall be directed toward those associations formed to create "new business" activity. Thus, a joint venture⁹ for our purposes is defined as an association between corporate entities for pooling of resources and skills through incorporation of a joint subsidiary to conduct a new business enterprise. This definition *excludes* joint involvement through merger or consolidation, exchange of stock, and acquisition of stock or assets in an established corporation.¹⁰

Creation of a joint subsidiary establishes varying identifiable relationships between the venture and the parent companies. Joint ventures have been classified as horizontal, vertical, conglomerate, or a combination thereof. An understanding of the differences in these relationships is helpful in analyzing the major problems to be discussed, including anticompetitive effects, analogy to mergers, and potential competition.

A "horizontal joint venture" results when two or more actual or potential competitors create a new enterprise to produce or sell the same product as the parents produce or sell, but in a different geographical market. The parents thus form the horizontal venture to exploit a new or third geographical area where neither presently participates.¹¹

lines of commerce many of which "were integral parts of a world-wide cartel." Contrasting these multi-headed giants "decked out in the garb of a joint venture," recognition was given to the necessity in some cases for small, individually insignificant, companies to band together through joint arrangements to meet certain competitive situations. Between these two extremes lies the *Penn-Olin* case, which is worthy of considerable discussion. *United States v. Penn-Olin Chem. Co.*, 217 F. Supp. 110 (D. Del. 1963), *remanded*, 378 U.S. 158 (1964), 246 F. Supp. 917 (D. Del. 1965), *aff'd without opinion*, 389 U.S. 308 (1967). Of particular interest is the divergence of approaches found in the Dixon speech and by the Department of Justice when contrasted with that of the District Court in its exhaustive treatment of the record. Dixon, *Joint Ventures: What is Their Impact on Competition?*, 7 ANTITRUST BULL. 397 (1962).

⁹ The terms joint venture, joint subsidiary, and corporate joint venture will be used interchangeably herein unless otherwise distinguished.

¹⁰ The stock of a corporate joint venture is wholly owned by two or more other corporations. It is to be distinguished from wholly-owned subsidiaries, and the term is not usually applied to a company which is partially owned by other corporations and partially owned by the public. Section 7 of the Clayton Act, 15 U.S.C. § 18 (1964), does not reach a joint association composed of individuals. See Backman, *Joint Ventures and the Antitrust Laws*, 40 N.Y.U.L. REV. 651 (1965); Berghoff, *Antitrust Aspects of Joint Ventures*, 9 ANTITRUST BULL. 231 (1964); Hale, *Joint Ventures: Collaborative Subsidiaries and the Antitrust Laws*, 42 VA. L. REV. 927 (1956); cf. Nichols, *Joint Ventures*, 36 VA. L. REV. 425 (1950).

¹¹ A joint venture formed to produce or sell a product that both parents produce or sell in an area of existing competition between the parents, while technically creating a new entity and new competitive force, is so similar to a horizontal merger with foreclosure of actual competition, that it cannot be considered a "new business" joint venture.

A "vertical joint venture" operates at a different functional level than that of the parents. The "backward vertical venture" establishes a new entity which acts as a source of supply for the parent corporations which typically will be competitors in their product market. The "forward vertical venture" creates a new entity which will become a customer of the parent corporations, typically buying exclusively from them.¹² The relationship of the parents may be competitive or non-competitive depending on the nature of their separate existences.

The "conglomerate venture" occurs when two or more corporations create a new entity to engage in an enterprise entirely different from those previously engaged in by the respective parents. It is distinguished from vertical and horizontal ventures in that this entity is neither customer, supplier, nor competitor of any participating parent.

A "mixed" joint subsidiary is a combination of the above relationships; the variations are too numerous to list. The many possible combinations serve to point up the dubious value of labeling and broad generalizations with respect to joint ventures, unless the class of relationships and factual background is clearly understood.¹³

Joint Ventures and Merger Rationale. Any discussion of applicability of antitrust laws to joint ventures suggests an inquiry into the established judicial precedents found in merger situations. Both mergers and joint ventures are the result of two distinct business entities joining together in a common business endeavor. The distinctive feature of a joint venture is the creation of a new productive organization with the parents' identities left intact. Mergers eliminate the corporate existence of one or more of the parents.¹⁴

Elimination of the corporate existence of one of the parents through merger may or may not reduce the number of competitors in a particular geographic or product market. A horizontal merger reduces the number of competitors by one or more, while vertical and conglomerate mergers tend to leave the number unchanged. A new business joint venture always increases the number of *actual*¹⁵ competitors in a field and tends to in-

¹² Texas-U.S. Rubber Chemical Company provides an example of a venture that occupies a forward vertical position with one parent and a backward vertical relation with the other. It manufactures synthetic rubber with some raw material requirements from Texas Company (now Texaco, Inc.) and sells its output to U.S. Rubber Company. The venture is thus a customer to one parent and an assured source of supply to the other. The facilities were purchased from the United States Government with direct involvement by Congress and the Department of Justice. See Boyle, *The Joint Subsidiary: An Economic Appraisal*, 5 ANTITRUST BULL. 303, 310-11 (1960). See also *Ethyl Gasoline Corp. v. United States*, 309 U.S. 436 (1940). For discussion of disposal of Government-owned synthetic rubber facilities to joint venturers, see Comment, *Joint Subsidiaries and Section 7 of the Clayton Act*, 39 DET. L.J. 223, 230-35 (1961).

¹³ See Tractenberg, *supra* note 3; Comment, *The Corporate Joint Venture Under the Antitrust Laws*, 37 N.Y.U.L. REV. 712 (1962); Comment, *Corporate Joint Ventures and Section 7 of the Clayton Act*, 9 VILL. L. REV. 94 (1963).

¹⁴ "In a merger, two or more companies combine *all* of their assets to create a new entity. In a joint venture, two or more companies combine *less than all* of their assets to create a new entity." Bernstein, *Joint Ventures in the Light of Recent Antitrust Developments: Anti-Competitive Joint Ventures*, 10 ANTITRUST BULL. 25 (1963).

¹⁵ While joint ventures increase the number of actual competitors, they may decrease the number of potential competitors by one or more. This will be discussed fully in a separate section, *infra*, notes 117-25, and accompanying text.

crease the number of customers available to suppliers and the number of outlets available to consumers.¹⁶ A merger often reduces the number of customers available to suppliers and the number of choices available to consumers.

While analogy to horizontal, vertical, and conglomerate mergers is both useful and inevitable, such an analysis should not lose sight of the fact that a new business joint venture creates a new entity, while mergers extinguish an entity. Understanding the ramifications of this distinction is essential in making the ultimate determination—effect on competition.

Joint Ventures: Economic Motive vs. Anticompetitive Effect. The economic advantages accruing to parents of a joint enterprise are easily stated and have contributed substantially to the popularity of this form of doing business. They are to (1) provide the large amounts of capital needed for development of raw materials and natural resources, (2) increase chances of success of a technological innovation with uncertain prospects and considerable capital requirements, (3) establish one large facility in the production or marketing chain which is more economical and efficient in operation than smaller, separate installations, and (4) undertake research projects on a scale too vast for single companies.

Perhaps the strongest motivation prompting our society to change from one dependent upon sole proprietorships to one dependent upon business associations was the desire of individuals to band together to increase their ability to raise capital and share unusual risks. As corporations have become more sophisticated, merger waves have periodically swept the country, prompted in many cases by the additional advantages of complementary use of research and marketing techniques and by economies of vertical integration. These same basic economic advantages today motivate corporations large and small—whether consummated in joint subsidiary form or not—to join together.

The many compelling and laudable reasons for creating joint ventures are not sufficient in and of themselves to justify venture creation in many cases. The real antitrust problems center around what has been characterized as the power motive—the desire to lessen or avoid competition—and those situations where the necessary or probable result will be a substantial lessening of competition.¹⁷ Preoccupation with classifying labels (horizontal, vertical, conglomerate or mixed) is not likely to be fruitful in making these determinations. Anticompetitive effects and public injury should be assayed only after a thorough examination of a venture in its particular setting, as will be later demonstrated.

¹⁶ "It is evident, therefore, that the formation of a joint venture in terms of numbers must, in the first instance, add a new dimension to competition and the size of the market." Backman, *Joint Ventures in the Light of Recent Antitrust Developments: Joint Ventures in the Chemical Industry*, 10 ANTITRUST BULL. 7, 9 (1965).

¹⁷ Berghoff, *supra* note 10, at 233; Boyle, *supra* note 12, at 307; Handler, *Emerging Antitrust Issues: Reciprocity, Diversification and Joint Ventures*, 49 VA. L. REV. 433, 442 (1963); Tractenberg, *supra* note 3, at 805; Comment, *The Joint Venture Meets Section 7 of the Clayton Act: Technical Capability, Reasonable Probability and Business Reality*, 38 S. CAL. L. REV. 104, 108 (1965).

In addition to the criticism of joint ventures as a mere convenience device to avoid the rigors of independent competition by the parents, other possible anti-competitive effects have been stated. One is that price, production, and other decisions of the parents—for themselves and their progeny—may be so interrelated that the results will be altered substantially and will affect adversely competition in a manner which would not occur if the venture were independent of the parents. This risk is most likely to occur when the venture produces the same goods as its parents.¹⁸

The charge has been made that acting as a joint venture at one level—for example, manufacturing or mining—may well lead to collateral restrictive behavior at another level, such as retailing or in another line of commerce. The fear is that when actual or potential competitors are afforded a common meeting ground to discuss venture matters, a myriad of collaborative practices, such as reduction in competition between the parents' independent facilities or restrictive elimination of competition between the parents and the venture, may result.¹⁹

Other criticisms include the assertions that entry by way of joint venture into a line of commerce will raise entry barriers for small corporations, that a leading potential competitor may be eliminated by absorption into a joint venture, and that substantial power possessed by one or more of the parents in one market may be used to create similar and stifling power in the venture market.²⁰

II. JOINT VENTURES AND THE SHERMAN ACT

Basic Prohibitions. While there is no inherent illegality in engaging in joint ventures, there is no question that they are and should be subject to sections 1 and 2 of the Sherman Act.²¹ The purpose of the Sherman Act is "to protect trade and commerce against unlawful restraints and monopolies."²² Section 1 prohibits contracts, combinations, or conspiracies in restraint of trade.²³ Section 2 declares it unlawful for any person to monopolize trade, attempt to monopolize trade, or combine or conspire to mo-

¹⁸ C. KAYSER & D. TURNER, ANTITRUST POLICY 138 (1959). "One of the anticompetitive dangers of joinder inheres in the fact that the creation of a venture by two previously independent corporations results in a triumvirate of associated corporations." Note, *Applicability of Section 7 to a Joint Venture*, 11 U.C.L.A.L. REV. 393, 396 (1964).

¹⁹ *United States v. Minnesota Mining & Mfg. Co.*, 92 F. Supp. 947, 963 (D. Mass. 1950); Comment, *supra* note 17, at 108.

²⁰ See *FTC v. Procter & Gamble Co.*, 386 U.S. 568 (1967); C. KAYSER & D. TURNER, *supra* note 18, at 138; Bernstein, *supra* note 14; Dixon, *supra* note 8.

²¹ *United States v. Penn-Olin Chem. Co.*, 378 U.S. 158 (1964); *Timken Roller Bearing Co. v. United States*, 341 U.S. 593 (1951); *United States v. Paramount Pictures, Inc.*, 334 U.S. 131 (1948); *United States v. National Lead Co.*, 332 U.S. 319 (1947); *Associated Press v. United States*, 326 U.S. 1 (1945); *United States v. Terminal R.R. Ass'n*, 224 U.S. 383 (1912); *United States v. American Tobacco Co.*, 221 U.S. 106 (1911); *United States v. Pan Am. World Airways, Inc.*, 193 F. Supp. 18 (S.D.N.Y. 1961), *remanded on other grounds*, 371 U.S. 296 (1963); *United States v. E.I. du Pont de Nemours & Co.*, 118 F. Supp. 41 (D. Del. 1953), *aff'd on other grounds*, 351 U.S. 377 (1956); *United States v. Imperial Chem. Indus., Ltd.*, 100 F. Supp. 504 (S.D.N.Y. 1951); see dictum in *United States v. Minnesota Mining & Mfg. Co.*, 92 F. Supp. 947, 963 (D. Mass. 1950).

²² Sherman Act, 15 U.S.C. § 1 (1964).

²³ "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal:" 15 U.S.C. § 1 (1964).

nopolize trade.²⁴ However, no definitions of specific misconduct can be found in the Act.²⁵ This lack of preciseness makes it incumbent on the judiciary to give the Sherman Act meaning to the business community.

Tests of Legality. The Sherman Act does not contain a reasonableness standard, and early cases rejected such a standard, holding that no exception or limitation could be adduced without writing into the Act what Congress had omitted.²⁶ The Supreme Court in 1911, however, in the leading case of *Standard Oil of New Jersey v. United States*²⁷ carefully examined the history and philosophy behind enactment of the Sherman Act, and concluded that only those agreements and combinations which prejudice public interest by *unduly* restricting competition or *unduly* obstructing the due course of trade are embraced by it.²⁸

As a result of extended judicial experience with the Sherman Act, certain agreements and practices which have a "pernicious effect on competition and lack of any redeeming virtue"²⁹ are now presumed unreasonable without elaborate inquiry into factual circumstances or economic data. Per se unreasonable categories include price fixing,³⁰ division of markets,³¹ group boycotts,³² and product tying arrangements.³³

Application of the "rule of reason" prevails in joint venture cases, as it is clear that the mere fact of joint venturing does not give rise to a per se violation of the Act.³⁴ It does not follow, however, that joint ventures

²⁴ "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 misdemeanor . . ." 15 U.S.C. § 2, at 336 (1964).

²⁵ *Standard Oil Co. v. United States*, 221 U.S. 1, 59-60 (1911): "In view of the many new forms of contracts and combinations which were being evolved from existing economic conditions, it was deemed essential by an all-embracing enumeration to make sure no form of contract or combination by which an undue restraint of interstate or foreign commerce was brought about could save such restraint from condemnation." See Handler, *The Judicial Architects of the Rule of Reason*, 10 ABA ANTITRUST SECTION 21 (1957).

²⁶ *United States v. Joint Traffic Ass'n*, 171 U.S. 505 (1898); *United States v. Trans-Missouri Freight Ass'n*, 166 U.S. 290 (1897).

²⁷ 221 U.S. 1 (1911).

²⁸ The Act "being broad enough to embrace every conceivable contract or combination which could be made concerning trade or commerce . . . [and cause] any act done . . . in the whole field of human activity to be illegal if in restraint of trade, it inevitably follows that . . . [it calls] for the exercise of judgment . . . Thus not specifying but indubitably contemplating and requiring a standard, it follows that it was intended that the standard of reason . . . was intended to be the measure used" in determining violations of the Act. *Id.* at 60; Thomsen v. Caysner, 243 U.S. 66, 84 (1917); see Bork, *The Rule of Reason and the Per Se Concept: Price Fixing and Market Division*, 75 YALE L.J. 373 (1966); Montague, "Per se Illegality" and the Rule of Reason, 12 ABA ANTITRUST SECTION 69 (1958).

²⁹ "This principle . . . avoids the necessity for an incredibly complicated and prolonged economic investigation into the entire history of the industry involved, as well as related industries, in an effort to determine at large whether a particular restraint has been unreasonable—an inquiry so often wholly fruitless when undertaken." *Northern Pac. Ry. v. United States*, 356 U.S. 1, 5 (1958); See generally Van Cise, *The Future of Per Se in Antitrust Law*, 50 VA. L. REV. 1165 (1964).

³⁰ *United States v. Socony Vacuum Oil Co.*, 310 U.S. 150 (1940).

³¹ *United States v. Addyston Pipe & Steel Co.*, 85 F. 271 (6th Cir. 1898), *aff'd*, 175 U.S. 211 (1899).

³² *Fashion Originators' Guild of America, Inc. v. FTC*, 312 U.S. 457 (1941).

³³ *International Salt Co. v. United States*, 332 U.S. 392 (1947).

³⁴ *United States v. Pan Am. World Airways, Inc.*, 193 F. Supp. 18, 48 (S.D.N.Y. 1961); *United States v. E.I. du Pont de Nemours & Co.*, 118 F. Supp. 41, 219-20 (D. Del. 1953),

formed for the purposes or having the effects prohibited in the per se unreasonable classifications would escape judicial wrath. The vital distinction between per se situations and new business joint ventures is that the latter create a new competitive force, and thus are entitled to closest scrutiny before being found unreasonable. A substantial majority of writers in the field support the "rule of reason" approach to joint ventures.³⁵

Applicability to Joint Ventures. In applying the reasonableness standard to specific cases, the courts have found it necessary to inquire whether a given restraint "merely regulates and perhaps thereby promotes competition or whether it is such as may suppress or even destroy competition."³⁶ It is necessary to consider the actual or probable nature of the restraint, the particular factual setting to which it is applied, the business conditions before and after it was imposed, and the purpose or result sought to be attained. The factors relevant in determining the reasonableness of one venture may or may not be relevant in examining another venture.³⁷

The district court decision in *United States v. Pan American Airways*,³⁸ involving an admitted division of territories among the venture parents, provides a strong example of Sherman Act sufficiency and vitality in testing new business joint ventures and the inappropriateness of per se classifications with respect to them. In 1929, Pan American World Airways and W.R. Grace & Company formed a jointly owned subsidiary, Pan American-Grace Airways (Panagra) for the purpose of operating an airline along the west coast of South America. The complaint, filed some thirty years later, charged unlawful conspiracy in restraint of trade and division of markets in the transportation of passengers, cargo, and mail between the United States and South America both from the standpoint of reasonableness and as a per se violation of section 1, and charged an attempt to monopolize such transportation in violation of section 2.

In 1927, international commercial aviation was in the experimental stage; no American air transportation was in operation between the United States and South America and substantially all transportation was by steamship. Late in 1927, Pan American began to formulate plans to enter the South American market, but its ambitions were not equalled by its

aff'd, 351 U.S. 377 (1956); *United States v. Imperial Chem. Indus., Ltd.*, 100 F. Supp. 504, 557 (S.D.N.Y. 1951).

³⁵ K. BREWSTER, *ANTITRUST AND AMERICAN BUSINESS ABROAD* 206 (1958); W. FUGATE, *FOREIGN COMMERCE AND THE ANTITRUST LAWS* 257 (1958); REPORT OF ATTORNEY GENERAL'S NATIONAL COMMITTEE TO STUDY ANTITRUST LAWS 90 (1955); Boyle, *supra* note 12, at 310; Friedmann, *Antitrust Law and Joint International Business Ventures in Economically Underdeveloped Countries*, 60 COLUM. L. REV. 780, 790 (1960); Tractenberg, *supra* note 3, at 804; Comment, 37 N.Y.U.L. REV., *supra* note 13, at 714. *But see* Graham, *Antitrust Problems of Corporate Parents, Subsidiaries, Affiliates and Joint Ventures in Foreign Commerce*, 9 A.B.A. SECTION OF ANTITRUST L. PROC. 32, 38 (1956).

³⁶ "To determine that question the court must ordinarily consider the facts peculiar to the business to which the restraint is applied; . . . the nature of the restraint and its effect, actual or probable. The history of the restraint, the evil believed to exist, the reason for adopting the particular remedy, the purpose or end sought to be attained, are all relevant facts." *Board of Trade v. United States*, 246 U.S. 231, 238 (1918).

³⁷ *Id.*; *Jewel Tea Co. v. Local Unions*, 274 F.2d 217 (7th Cir. 1960); *United States v. Twentieth Century Fox Film Corp.*, 137 F. Supp. 78 (S.D. Cal. 1955).

³⁸ 193 F. Supp. 18 (S.D.N.Y. 1961).

assets and financial resources. In early 1928, Grace independently began inquiry into the feasibility of establishing an airline to the west coast of South America, the only area where its steamships faced air competition at that time. The key to successful maintenance of an American airline in South America was a United States postal contract, without which any company would suffer heavy losses. With bids on postal contracts pending, Grace and Pan American held meetings in 1928 which culminated in formation of Panagra. Their joinder, with their complementary resources, was of decisive importance in awarding the postal contract to Panagra.

From the outset, each parent fully appreciated the dangers of competition between themselves for the mail contract, and Grace was concerned particularly about the potential competition of air transportation with its large steamship investments. Each parent, while in a strong bargaining position, needed the attributes of the other for the successful operation of the airline, and each feared the consequences of the other's opposition.³⁹

After reviewing all of the evidence, the court concluded that *formation* of Panagra did not constitute a conspiracy in restraint of trade:

The joinder of Grace and Pan American of their complementary facilities was a natural and mutually advantageous combination, and an economically sound arrangement for the establishment and successful development of American commercial aviation on the west coast of South America. . . . The union of their physical and technical resources assured the maximum possibilities of success in instituting and carrying on a pioneering venture, useful to the community which did not theretofore exist.⁴⁰

With the purpose of the combination found legitimate, the court pointed out that "differences of opinion as to the growth and development of their jointly owned company does not . . . operate to make their joinder or combination, *in limine*, one in restraint of trade, or their combination presently, *qua* combination, one in restraint of trade."⁴¹

The crux of the suit revolved around Grace's nominees' attempts to broaden the venture scope of operation after it began to prosper. Beginning in 1938, the Grace nominees sought to extend Panagra's routes, formerly confined strictly to South America, to the United States in competition with Pan American. Pan American, by reason of its fifty per cent stock ownership in Panagra, negatively blocked the competition; this veto ultimately led to suit being filed.

A very important aspect of the case was the court's demonstration of applicability of section 2 to joint ventures, and appropriate remedies

³⁹ By joining with each other in a joint venture on the west coast, Grace on the one hand would be assured against the entry of an independent American airline competitor in its west coast domain, and gain time to acquire the experience and know-how of this new industry. . . . Pan American on the other hand would be substantially free from American flag competition in the rest of Latin America. Their method of organization of the joint company appears calculated to give each negative control of the company to insure against the possible treachery of the other to expand the operations of the company in competition with their respective independent lines

Id. at 31.

⁴⁰ *Id.* at 32-33.

⁴¹ *Id.* at 38.

thereunder. The court assumed, as pointed out above, that Pan American came by its virtual monopoly position legally, but found that Pan American's use of its position to frustrate Panagra's entry into the market contravened section 2 of the Sherman Act. Thus Pan American was ordered to show cause why it should not be divested of its interest in Panagra.

The court further noted (1) that Pan American's justification for blocking the venture's efforts was based on fallacious predicate since Panagra was *not* part of the Pan American system, and (2) that the venture's abstention from independent entry was not the result of *concerted* action. Demonstrating a proper understanding of the "rule of reason" approach to joint venture cases, the court stated: "We would like it clearly understood that it is not our opinion that every defendant who exercises similar negative control over a single potential competitor and thereby excludes such competitor from a relevant market necessarily monopolizes thereby. *It is a relative concept which can only be applied in a given context.*"⁴²

By reason of the conceded division of markets, the Government was not content to confine its efforts to the restraining parent, and charged that the mere ownership or control by a steamship company of an airline company operating a parallel route constitutes a *per se* violation of section 1. In commenting on the Government's citations of authority "where the obvious purpose was to eliminate competition,"⁴³ the court made the proper distinction vital to new business ventures: "It is apparent that the principle upon which these cases were decided applied to combinations of existing companies *which were in substantial competition with one another prior to their combination,*"⁴⁴ and properly concluded that Grace's ownership of Panagra did not have such a "pernicious effect on competition and lack of any redeeming virtue" that it constituted *per se* unreasonable restraint on trade and commerce.

It is most unfortunate that on appeal to the Supreme Court,⁴⁵ the excellent analysis and holdings of the district court were muddled by the higher court's involvement with "primary jurisdiction" of the Civil Aeronautics Board, which did not reach the merits of the antitrust issues. The district court's decision remains, however, a compelling testament to the complete sufficiency of Sherman Act concepts and remedies in dealing with new business joint ventures. Furthermore, that decision should be understood to have application to venture problems from inception through abuse, and not be categorized as a mere "pioneering venture" case.

Another case which applied the "rule of reason" approach to joint ventures was *United States v. Imperial Chemical Industries*,⁴⁶ where the court found the major purpose of agreements between the parents for formation of joint manufacturing subsidiaries with exchange of patents and pro-

⁴² *Id.* at 41 (emphasis added).

⁴³ *Id.* at 48.

⁴⁴ *Id.* (emphasis added).

⁴⁵ *United States v. Pan Am. World Airways, Inc.*, 371 U.S. 296 (1963).

⁴⁶ *United States v. Imperial Chem. Indus., Ltd.*, 100 F. Supp. 504 (S.D.N.Y. 1951).

cesses was for division of world markets and avoidance of competition in the manufacture of explosives. The proof showed that the American parent, which was already established in a foreign market, and the British parent, which had a foothold in the same market, combined for the purpose of developing the market to their mutual benefit with profits divided on an agreed basis. These agreements were found unreasonable in violation of section 1, but the court stated: "It is settled that joint manufacturing ventures, even in domestic markets, are not made unlawful per se by the Sherman Act, but become unlawful only if their purpose or their effect is to restrain trade or to monopolize."⁴⁷

Although the district court went overboard with gratuitous dictum, *United States v. Minnesota Mining & Manufacturing Co.*⁴⁸ further illustrates how the Sherman Act is more than adequate to control abuses under a joint venture arrangement. For reasons of market protection, American manufacturers controlling four-fifths of the export trade in coated abrasives agreed not to compete in areas supplied by their jointly owned foreign subsidiaries. The restraint was not the mere formation of the joint subsidiaries, but the agreement not to compete with them when it was legally, politically, and economically possible to do so. In a statement that must be considered in context, the court conjectured that:

It may very well be that even though there is an economic or political barrier which entirely precludes American exports to a foreign country a combination of dominant American manufacturers to establish joint factories for the sole purpose of serving the internal commerce of that country is a *per se* violation . . . of the Sherman Act. The intimate association of the principal American producers in day-to-day manufacturing operations, their exchange of patent licenses and industrial know-how, and their common experience in marketing and fixing prices may inevitably reduce their zeal for competition *inter sese* in the American market.⁴⁹

Keeping in mind that the court was dealing with a combination controlling eighty per cent of an export market, this dictum does nothing to dilute other holdings taking a "rule of reason" approach to joint ventures. The disturbing language relates to the presumption that anticompetitive business *attitudes* will flow from joint involvement. As stated by the district court in *United States v. Penn-Olin Chemical Co.*, "[t]o equate opportunity for wrongdoing with likelihood of its occurrence reflects a cynicism toward business behavior which is without warrant. Presumption of probable wrongdoing cannot be a substitute for its proof."⁵⁰

The belief that new business joint ventures are sophisticated devices which enjoy some degree of immunity under Sherman Act standards is amply put to rest by *Timken Roller Bearing Co. v. United States*.⁵¹ Although "new business" was not involved in *Timken*, the case can easily be extended to new ventures formed for the same purposes as the ven-

⁴⁷ *Id.* at 557, citing *United States v. Columbia Steel Co.*, 334 U.S. 495 (1948).

⁴⁸ 92 F. Supp. 947 (D. Mass. 1950).

⁴⁹ *Id.* at 963.

⁵⁰ 217 F. Supp. 110, 134 (D. Del. 1963).

⁵¹ 341 U.S. 593 (1951).

ture in *Timken*. Timken, an American manufacturer of anti-friction bearings, owned a substantial interest in a British competitor. Together they acquired the stock of a French company which was a going concern and produced the same product. The district court found that under agreements between them, the three corporations allocated trade territories, fixed prices on products of one corporation sold in the territory of the others, cooperated to protect each other's markets and eliminate outside competition, and participated in cartels to restrict imports to, and exports from, the United States which was clearly illegal under the Sherman Act.⁵²

Before the Supreme Court, the defendants contended that any restraints of trade could be justified as "reasonable" and not violations of the Sherman Act because they were ancillary to an otherwise legal joint venture. The court summarily rejected this contention, stating:

The fact that there is common ownership or control of the contracting corporations does not liberate them from the impact of the antitrust laws. . . . Nor do we find any support in reason or authority for the proposition that agreements between legally separate persons and companies to suppress competition among themselves and others can be justified by labeling the project a 'joint venture.' Perhaps every agreement and combination to restrain trade could be so labeled.⁵³

Effect of Motives and Injury to Public. Courts have been cognizant since the enactment of the Sherman Act that various attempts would be made by the business community to circumvent its prohibitions to the detriment of the public interest in maintaining a free enterprise system.⁵⁴ In order for a venture to survive the "rule of reason" test, the benefits which will accrue to the public, directly or indirectly, must outweigh any anticompetitive effects created by the venture.⁵⁵ Basically, this balancing involves the assessment of potential advantages and disadvantages in joint ventures from the point of view of the public interest and the determination of what characteristics are likely to produce a balance one way or the other.

⁵² Justice Frankfurter warned in his dissenting opinion that "[e]ven 'cartel' is not a talismanic word, so as to displace the rule of reason by which breaches of the Sherman Law are determined. Nor is 'division of territory' so self-operating a category of Sherman Law violations as to dispense with analysis of the practical consequences of what on paper is a geographic division of territory." *Timken Roller Bearing Co. v. United States*, 341 U.S. 593, 605 (1951).

⁵³ *Id.* at 598. Additional cases on conspiracy between a parent corporation and its subsidiary include: *Kiefer-Stewart Co. v. Joseph E. Seagram & Sons, Inc.*, 340 U.S. 211 (1951); *United States v. Columbia Steel Co.*, 334 U.S. 495 (1948); *Schine Chain Theatres, Inc. v. United States*, 334 U.S. 110 (1948); *United States v. Yellow Cab Co.*, 332 U.S. 218 (1947); *United States v. General Motors Corp.*, 121 F.2d 376 (7th Cir.), *cert. denied*, 314 U.S. 618 (1941). See also REPORT OF ATTORNEY GENERAL'S NATIONAL COMMITTEE TO STUDY ANTITRUST LAWS 34-35 (1955); Sprunk, *Intra-Enterprise Conspiracy*, 9 ABA ANTITRUST SECTION 20 (1956).

⁵⁴ As forcefully stated in the 1911 *American Tobacco* case, the generic designation of the first and second sections of the law, when taken together, embraced every conceivable act which could possibly come within the spirit or purpose of the prohibitions of the law, without regard to the garb in which such acts were clothed. That is to say, it was held that in view of the general language of the statute and the public policy which it manifested, there was no possibility of frustrating that policy by resorting to any disguise or subterfuge of form

United States v. American Tobacco Co., 221 U.S. 106, 181 (1911).

⁵⁵ *Sandidge v. Rogers*, 167 F. Supp. 553 (S.D. Ind. 1958); *Tractenberg*, *supra* note 3, at 805.

Public injury is not a separate and distinct element which must be shown before a violation of the Sherman Act can be found,⁵⁶ but is part of the test of unreasonable restraint of trade. If a venture is tested under Sherman Act standards, and tends or is reasonably calculated to prejudice the public interest, it will be forbidden as unreasonably restraining trade.⁵⁷

Examples of joint ventures which could be declared unlawful under the Sherman Act are those formed for the purpose or having the effect of the following types of public injury: Obstructing interstate commerce,⁵⁸ increasing costs and declining services,⁵⁹ imposing an economic burden on the public by controlling or increasing prices,⁶⁰ limiting the availability of a product to the public by restricting production,⁶¹ dividing markets,⁶² and possessing such undue market power as to eliminate or seriously lessen competition.⁶³

In summary, a joint venture should be condemned only upon specific proof that by reason of intent of the parents or by the inherent nature of the venture, it will prejudice the public interest by unduly restricting competition or unduly obstructing the due course of trade.⁶⁴ The question is basically one of fact. Where the true motive behind the venture is furtherance of an anticompetitive advantage, a violation of the Sherman Act should be found.⁶⁵ Generally, good intentions or motives are irrelevant. If the *necessary result* of a joint venture is to restrain trade, the intent with which the venture was formed is of no consequence.⁶⁶ However, where there is only a *probability* of trade restraint, lack of anti-

⁵⁶ *Radiant Burners, Inc. v. Peoples Gas Light & Coke Co.*, 364 U.S. 656 (1961); *Klor's, Inc. v. Broadway-Hale Stores*, 359 U.S. 207 (1959); *Switzer Bros. v. Locklin*, 297 F.2d 39 (7th Cir. 1961); *Syracuse Broadcasting Corp. v. Newhouse*, 295 F.2d 269 (2d Cir. 1961).

⁵⁷ *Rogers v. Douglas Tobacco Board of Trade, Inc.*, 266 F.2d 636, 644 (5th Cir. 1959). "Appellees seem to make some distinction between an unreasonable restraint and the principle that the public rights must be violated before an offense is committed. These are merely different ways of saying the same thing." *Lynch v. Magnavox Co.*, 94 F.2d 883, 891 (9th Cir. 1938).

⁵⁸ *Bankers Life & Cas. Co. v. Larson*, 257 F.2d 377 (5th Cir. 1958).

⁵⁹ *Parmelee Transp. Co. v. Keeshin*, 144 F. Supp. 480 (N.D. Ill. 1956).

⁶⁰ *Addyston Pipe & Steel Co. v. United States*, 175 U.S. 211 (1899); *Riggall v. Washington County Medical Soc'y*, 249 F.2d 266 (8th Cir. 1957). *But see Bork, supra* note 28, at 461-64.

⁶¹ *Apex Hosiery Co. v. Leader*, 310 U.S. 469 (1940).

⁶² *Timken Roller Bearing Co. v. United States*, 341 U.S. 593 (1951); *United States v. National Lead Co.*, 332 U.S. 319 (1947) (division of titanium market); *United States v. American Tobacco Co.*, 221 U.S. 106 (1911); *United States v. Imperial Chem. Indus., Ltd.*, 100 F. Supp. 504 (S.D.N.Y. 1951); *United States v. Minnesota Mining & Mfg. Co.*, 92 F. Supp. 947 (D. Mass. 1950); *United States v. General Elec. Co.*, 82 F. Supp. 753 (D.N.J. 1949) (cartel arrangements in the electric light industry); *see W. FUGATE, supra* note 35, at 258; *C. KAYSER & D. TURNER, supra* note 18, at 136.

⁶³ *United States v. Paramount Pictures, Inc.*, 334 U.S. 131 (1948); *Associated Press v. United States*, 326 U.S. 1 (1945) (non-association newspapers were permitted to join on reasonable terms); *United States v. Terminal R.R. Ass'n*, 224 U.S. 383 (1912) (a joint venture terminal which controlled railroad access was required to permit other railroads to utilize the venture facilities on a non-discriminatory basis); *American TCP Corp. v. Shell Oil Co.*, 127 F. Supp. 208 (S.D.N.Y. 1955).

⁶⁴ *Thomsen v. Cayser*, 243 U.S. 66 (1917); *Standard Oil Co. v. United States*, 221 U.S. 1 (1911); *C. KAYSER & D. TURNER, supra* note 18, at 137.

⁶⁵ "It has long been established that the legality of the means selected to effectuate an unlawful purpose does not immunize those engaged in the conspiracy to accomplish it." *United States v. General Dyestuff Corp.*, 57 F. Supp. 642, 646 (S.D.N.Y. 1944).

⁶⁶ *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150 (1940); *United States v. Trenton Potteries Co.*, 273 U.S. 392 (1927); *Addyston Pipe & Steel Co. v. United States*, 175 U.S. 211 (1899).

competitive intent should become important.⁶⁷ Knowledge of intent can assist the court in interpreting facts and predicting probable results.⁶⁸

The Supreme Court recently held that the Clayton Act is applicable to new business joint ventures. For this reason, the importance of Sherman Act sanctions inevitably will diminish. The purpose of this analysis in some detail is to demonstrate the complete sufficiency of these sanctions to reach all conceivable forms of anticompetitive subterfuges which joint ventures may pose. The Sherman Act, through the "rule of reason" approach, is imbued with the necessary flexibility to deal with sophisticated challenges to healthy market conditions and could adequately protect public interest in curbing anticompetitive joint ventures without stifling those that will constructively contribute to the economy. The glaring inadequacies of section 7 of the Clayton Act in dealing with new competition will be amply developed with the purpose of advocating sole reliance on the Sherman Act in new business joint venture cases.

III. "PLOWING NEW GROUND": THE PENN-OLIN CASE

First District Court Decision. Penn-Olin is a new business joint venture organized on February 25, 1960, by Olin Mathieson Chemical Corporation and Pennsalt Chemical Corporation to produce and sell sodium chlorate in the Southeastern United States. Under their agreement each of the joint venturers owns fifty per cent of the stock of Penn-Olin, and each company is represented by an equal number of officers and directors. Penn-Olin constructed a plant at Calvert City, Kentucky, with a production capacity of over 25,000 tons of sodium chlorate per year at a cost in excess of six and one-half million dollars. Under the operating arrangement, Pennsalt personnel are involved primarily in the manufacturing function while Olin Mathieson personnel primarily perform the sales function for the venture. On January 6, 1961, the United States filed suit charging violation of section 1 of the Sherman Act and section 7 of the Clayton Act.

The Sherman Act segment of the complaint charged that the joint venture (1) was the outgrowth of a conspiracy between Pennsalt and Olin dating back to 1957 to divide and allocate markets so as to eliminate and avoid all competition between them in the production and sale of sodium chlorate, and (2) unreasonably restrained trade in both sodium chlorate and other competitive products of the parents.

Applicability of the Clayton Act was based on amended section 7 on the theory that concurrent acquisition by Pennsalt and Olin of stock in their new creation was tantamount to an indirect acquisition by each of the assets of the other. As passed in 1914, section 7 was limited to stock acquisitions and did not reach asset acquisitions. This obvious loophole

⁶⁷ *United States v. Reading Co.*, 226 U.S. 324 (1912). *But see* *United States v. First Nat'l Bank & Trust Co.*, 376 U.S. 665 (1964).

⁶⁸ *Board of Trade v. United States*, 246 U.S. 231 (1918); *United States v. Union Pac. R.R.*, 226 U.S. 61 (1912). "When a combination through its actual operation results in an unreasonable restraint, intent or purpose may be inferred; even though no unreasonable restraint may be achieved, nevertheless a finding of specific intent to accomplish such an unreasonable restraint may render the actor liable under the Sherman Act." *United States v. Columbia Steel Co.*, 334 U.S. 495, 525 (1948).

made it an ineffectual restraint on corporate *mergers* and ultimately led to enactment of the Celler-Kefauver Anti-Merger Act of 1950.⁶⁹ The contrast of the old section 7 with the new can be illustrated by italicizing the added language and bracketing the deleted language:

That no corporation engaged in commerce shall acquire directly or indirectly, the whole or any part of the stock or other share capital and *no corporation subject to the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets* of another corporation engaged also in commerce, where *in any line of commerce in any section of the country*, the effect of such acquisition may be [to] substantially *to* lessen competition, [between the corporation whose stock is so acquired and the corporation making the acquisition, or to restrain such commerce in any section or community,] or to tend to create a monopoly [of any line of commerce].⁷⁰

In response, the defendants denied the substantive allegations of the complaint and further asserted the inapplicability of the Clayton Act on the grounds that Penn-Olin was not "engaged also in commerce" at the time of its formation and stock acquisition by the parents. In the alternative defendants claimed that Penn-Olin was a subsidiary corporation and entitled to treatment as such under a separate paragraph of section 7 which had not been involved in litigation since original enactment in 1914.⁷¹

The Government's allegation of conspiracy in restraint of trade was based upon two agreements between the parents prior to the venture formation. In December 1957, the parents entered into a sales agreement to test the Southeastern market. Under this agreement Pennsalt made available to Olin 2,000 tons of sodium chlorate per year to be sold only to pulp and paper mills in the Southeast, except for one company which Pennsalt reserved the right to serve directly. By further agreement in February 1958, the parents agreed that neither would move independently into the Southeastern chlorate market without advising the other and further agreed to bring to each other's attention any unusual development which might make it desirable to proceed with production plans.⁷²

Unfortunately, the district court's first decision⁷³ did not face squarely the challenges before it, but proceeded to examine the facts *as if* section 7 were applicable. Thus, the Sherman Act allegations were disregarded because "the anticompetitive standard imposed by Section 7 . . . is less

⁶⁹ 15 U.S.C. § 18 (1964).

⁷⁰ 38 Stat. 731 (1914), *as amended*, 15 U.S.C. § 18 (1964).

⁷¹ This alternative will be discussed in full, *infra*, notes 142-47, and accompanying text.

⁷² The sales arrangement allocated geographical and consumer markets for the sale of sodium chlorate. Its effect was to bar Pennsalt from any exploration of the southeastern pulp market for itself. At the same time it kept Olin from selling in any of the remaining areas where Pennsalt competed. The division of territory thus undertaken was substantially carried forward into Penn-Olin.

The February 1958 production arrangement, while less tangible, effectively destroyed all remaining opportunities for competition. By agreeing to consult on future plans, and thereafter respecting that pledge, promising plans for independent Eastern production by Pennsalt and Olin were thwarted.

Post-Trial brief of the United States at 16, *United States v. Penn-Olin Chem. Co.*, 217 F. Supp. 110 (D. Del. 1963).

⁷³ *United States v. Penn-Olin Chem. Co.*, 217 F. Supp. 110 (D. Del. 1963).

stringent than that of the Sherman Act."⁷⁴ The court passed over the jurisdictional question of whether the venture was "engaged in commerce" at the time of the asserted indirect acquisition of assets, and further refused to consider whether Penn-Olin was entitled to subsidiary status under section 7. The three basic aspects of every proper section 7 case were set out: "[w]hether the effect of the joint venture: (1) May be to lessen substantially competition or tend to create a monopoly; (2) In any section of the country; (3) In any line of commerce."⁷⁵

While this standard can be concisely stated, the magnitude of the difficulties in making predictable interpretations cannot be over-emphasized. However, in *Penn-Olin* the parties greatly reduced the court's assumed task by stipulating that two lines of commerce were relevant: Sodium chlorate and calcium hypochlorite (one of five non-chlorate chemicals in which Pennsalt and Olin were actual competitors).⁷⁶

With respect to the relevant geographical market, the Government sought to establish a *national* market in which to measure competitive effects, while the defendants successfully prevailed in demonstrating that the realistic area of effective competition for Penn-Olin was the Southeastern market comprising fourteen states. Prior to the venture formation, Hooker Chemical Corporation and American Potash Chemical Corporation had a "virtual monopoly" in this area amounting to over ninety per cent of sodium chlorate sales, while Pennsalt accounted for slightly less than nine per cent of the production sold in that market.

In a very careful analysis of the issue, the district court found that Pennsalt, with its sole production facility in Portland, Oregon, could not compete effectively in the Southeast with respect to price, service, or assured source of supply.⁷⁷ Furthermore, the court found that producers east of the Rockies could not favorably compete with production facilities west of the Rockies.⁷⁸ Olin, having never produced sodium chlorate in the Southeast or elsewhere, was not an actual competitor of any of the market occupants.

With respect to the venture's status, the combination was found to be in the nature of a conglomerate joint venture.⁷⁹ The ultimate issue was whether this conglomerate combination resulted, or as a reasonable probability⁸⁰ would result, in a substantial lessening of competition or

⁷⁴ *Id.* at 115, citing *Brown Shoe Co. v. United States*, 370 U.S. 294, 329 (1962).

⁷⁵ 217 F. Supp. at 115.

⁷⁶ Chosen as a "guinea pig" to test competitive effects of related products. Competition in calcium hypochlorite was substantial in that the venture parents accounted for 88.8% of the national market.

⁷⁷ 217 F. Supp. at 120-21.

⁷⁸ *Id.* at 122. Contrast this finding with Rand Dixon's statement that Pennsalt was "an ambitious newcomer in this field in the East." Dixon, *supra* note 8, at 405.

⁷⁹ "The creation of Penn-Olin did not represent a combination of companies which were competing in the manufacture and sale of sodium chlorate in the southeastern market or elsewhere. Nor did it represent a combination of companies standing in the relationship of supplier and customer in the southeastern market or elsewhere. It was neither a vertical combination or a horizontal combination." 217 F. Supp. at 124.

⁸⁰ The final Senate Report on amended section 7 was explicit on maintaining a distinction between possibility and probability. "The use of these words ('may be') means that the bill, if enacted, would not apply to the mere possibility but only to the reasonable probability of the prescribed [*sic*] effect." S. REP. NO. 1775, 81st Cong., 2d Sess., at 6 (1950).

would tend to create a monopoly. The crux of the substantial lessening controversy centered around the Government's "novel and far reaching"⁸¹ argument that since Pennsalt and Olin *could* have competed on an individual basis, antitrust law *required* that they do so or not enter the market at all. This assertion ignores relevant economic factors relating to whether or not Pennsalt and Olin *would* have entered the relevant market individually,⁸² and clearly draws the line between conflicting antitrust philosophies.

The district court properly disposed of the Government's position, which if adopted would have sounded the death knell to all significant future contributions to the economy by joint ventures. According to the court, the government's theory "would substitute a conclusive presumption that *any* combination specified in Section 7 between companies having the overall capability to go into business alone has a pernicious effect on competition and lacks any redeeming virtue; it would make *any* such combination illegal per se. No precedent supports the Government's position and its lack of logic condemns it."⁸³ The Supreme Court did not disturb this eminently sound holding on appeal, which hopefully will and should forever put to rest the concept that new business ventures as such are subject to per se illegality attacks. As joint ventures are entitled to a "rule of reason" approach under the Sherman Act, they are entitled, at a minimum, to an examination of the relevant economic factors surrounding the venture in the market place under section 7.

Although Penn-Olin was basically a conglomerate venture, it was not without horizontal and vertical aspects. Prior to the venture formation, Pennsalt held 8.9 per cent of the relevant Southeastern market. Formation of Penn-Olin removed Pennsalt as an independent competitor in the Southeast. Ending the inquiry here would be as untenable as the Government's per se approach. Whether a venture will have forbidden horizontal effects under section 7 cannot be measured merely by looking at the resultant activities of the parents.⁸⁴ Pennsalt's relatively insignificant position in the Southeast with its attendant competitive disadvantages was replaced amply by creation of Penn-Olin. The competitive benefits in the relevant market far exceeded any competitive loss resulting from Pennsalt's elimination.⁸⁵

With respect to the possible vertical aspect of the venture, Olin was a substantial buyer of sodium chlorate from Hooker's Niagara Falls plant. These purchases fulfilled Olin's neighboring plant's requirement for the manufacture of sodium chlorite. The Government asserted that the ven-

⁸¹ 217 F. Supp. at 123.

⁸² *Id.* at 124.

⁸³ *Id.* The Court cited *United States v. E.I. du Pont de Nemours & Co.*, 118 F. Supp. 41, 219-20 (D. Del. 1953), *aff'd*, 351 U.S. 377 (1956) and pointed out that it is not per se illegal for *actual* competitors to form a joint venture under the Sherman Act, and that a determination of unreasonableness is essential to illegality. The Government's position is even more untenable by reason of Pennsalt and Olin not being actual competitors.

⁸⁴ 217 F. Supp. at 125. "The 1950 amendments made plain Congress' intent that the validity of such combinations was to be gauged on a broader scale: their effect on competition generally in an economically significant market." *Brown Shoe Co. v. United States*, 370 U.S. 294, 335 (1962).

⁸⁵ 217 F. Supp. at 125.

ture formation would make Olin a captive buyer from Penn-Olin, and thereby foreclose Hooker and other suppliers from obtaining this business from Olin. The district court found that the record before it gave no indication as to how Olin would resolve the conflicting considerations of being a fifty per cent owner in the venture and the inherent advantages of a "next door" supplier, but pointed out that regardless of this possible foreclosure, it would not diminish competition in the Southeast.⁸⁶ Even if we assume a forbidden vertical foreclosure would result from this aspect of the venture, a remedy better than invalidating the venture might be a decree preventing Olin from making purchases from its joint subsidiary. Since the venture provided a robust new competitor for its relevant market, it should not be condemned by a proven forbidden ancillary restraint in an unrelated market which is easily curable.

With respect to the existing competition between the parents in non-chlorate chemicals, calcium hypochlorite was selected to test possible restraints. The Government dusted off the old rusty saw that the common meeting ground provided by the venture setting would lead inevitably to discussions of all phases of the non-chlorate business, and that it would "defy human nature" for the parents to maintain their competitive zeal in the competing products. No evidence was presented of actual or threatened collusion. Thus, the Government again attempted to exalt mere possibility as a well from which substantial lessening of competition necessarily would flow, and conveniently overlooked the delineation between possibility and probability which has been acknowledged by the Supreme Court.⁸⁷

There is no question that a joint venture involving parents with competing products provides a forum more conducive to wrongdoing than luncheon clubs, country clubs, trade associations and the like, but mere opportunity is not enough. With no proof offered, the court had no basis to infer wrongdoing under either the Sherman Act or section 7. With the Southeast established as the relevant market, the horizontal and vertical effects found inconsequential, evidence of foreclosure of competition between parents' competing products found lacking, and the overall competitive situation in the Southeast clearly improved, the focal point of the Government's case became foreclosure of potential competition between the parents.

While a new business joint venture always increases by one the number of actual competitors, in many cases it reduces the number of potential competitors. At the time of venture formation, both Pennsalt and Olin had extensive knowledge pertaining to sodium chlorate. Pennsalt had been engaged in manufacture and sale for years. Olin had never been a

⁸⁶ *Id.* at 126. Although not a joint venture case, *United States v. National City Lines*, 186 F.2d 562 (7th Cir.), *cert. denied*, 341 U.S. 916 (1951), holds that stock ownership in a consuming corporation is illegal even though all parents are noncompetitive in nature. National City Lines was operating bus services in a number of cities. It sold preferred stock to the manufacturers of buses, tires, gasoline and other products consumed in rendering transportation services. This was held to violate the Sherman Act because rival manufacturers were foreclosed from making substantial sales to National.

⁸⁷ *Brown Shoe Co. v. United States*, 370 U.S. 294 (1962); *see id.* at 323 n.39.

commercial manufacturer, but had substantial sales contacts in the Southeast and elsewhere by reason of its patented bleaching process (requiring sodium chlorate) used by pulp and paper processors, and had developed substantially a feasible commercial production process. Neither parent had rejected completely the idea of individual entry at the time of venture formation, but both had grave doubts as to feasibility from a projected profit standpoint.

Both parents had suitable locations for building a plant, and financing would not have been a problem for either company. Each possessed the resources and general capabilities needed to enter the Southeast singly, and could have competed at a profit. The Government's contention was that but for the venture, the probabilities were that both parents would have entered alone. This contention, if properly proven, would be compelling from a policy standpoint of encouraging individual entry. Thus, the task of the court was to predict what actions the parents probably would have taken if the venture had not been created, and measure these predicted actions against the standard of substantial lessening of competition.

A key holding by the district court was that the capability of both parents to build plants and compete individually was of no *controlling* significance.⁸⁸ Capacity and interest present no more than a *possibility* of entry, and should be important only as factors considered in the overall determination of reasonable probability. The court conducted a thorough examination of the factual setting from which the venture emerged (including analysis of numerous staff reports containing recommendations and profit projections, prior agreements between Pennsalt and Olin, and testimony of company principals) and concluded as a matter of reasonable probability that *both* parents would not have entered the Southeast absent venture formation. With respect to the possibility of one parent entering the market individually, the district court imposed a strict burden of proof on the Government. "If Penn-Olin had the effect of keeping Pennsalt or Olin out of the southeastern market, it runs afoul of Section 7 only if competition generally in the Southeast will probably be substantially less under the joint entry by Pennsalt and Olin *via* Penn-Olin than it would have been if there had been individual entry by either Olin or Pennsalt."⁸⁹

The Government's argument that the venture must be automatically condemned if either parent would have entered, was characterized as cutting "the heart out of Section 7."⁹⁰ The court's position points up the inherent difficulty of applying an anti-merger statute to the creation of a new entity. Removal of an established entity, especially a horizontal one, provides a basis of assessing the competitive effects before and after the combination based on prior performance. As pointed out, "lessening" is a word of comparison, and the challenged transaction must be com-

⁸⁸ 217 F. Supp. at 130.

⁸⁹ *Id.* at 131.

⁹⁰ *Id.*

pared with what would have existed otherwise. Since actual competition was not reduced, but in fact substantially augmented, the Government was placed in the unenviable position of trying to prove that individual entry by either company would have increased the level of competition *more* than joint entry by the parents. This burden could not be overcome, thus leading to appeal to the Supreme Court.

The Supreme Court Opinion. Upon direct appeal of the district court's decision, the Supreme Court held that there was no violation of section 1 of the Sherman Act.⁹¹ However, in the most significant extension of section 7 of the Clayton Act since its enactment, the Supreme Court expressly held it applicable when two corporations create a joint venture to engage in a wholly new enterprise.⁹²

A primary departure from the district court's analysis centered on that court's conclusion that since it was not reasonably probable that *both* parents would have independently entered the market, there was not a substantial lessening of competition. According to the Supreme Court, "[t]here still remained for consideration the fact that Penn-Olin eliminated the potential competition of the corporation that might have remained at the edge of the market, continually threatening to enter."⁹³ The case was remanded for a determination of whether either one of the parents would have entered the market as a reasonable probability, while the other remained a significant potential competitor. This narrow holding seeks to determine whether the joint venture would provide substantially less stimulus to competition than if one parent entered the market and the other remained at the edge of the market. Such a determination forces a careful analysis of all possible market combinations for measuring competitive effects of the venture formation, but unfortunately requires inquiry into a hypothesis (one parent entering) upon a hypothesis (other parent remaining at the market's edge) to determine reasonable probability of substantial lessening of competition. The real criticism of the Supreme Court's opinion—other than its finding of applicability of section 7—is its attitude toward the problem of proof with respect to reasonable probability of entry. The Court cited all factors contained in the record which clearly established Pennsalt and Olin as potential entrants in the Southeast market,⁹⁴ and observed that "[u]nless we are going to require subjective evidence, this array of probability certainly reaches the prima facie stage."⁹⁵ The proposition advanced by the Court is that a technical capacity and interest in entry on the part of a potential competitor present a prima facie case that entry by that company is reasonably

⁹¹ United States v. Penn-Olin Chem. Co., 378 U.S. 158, 161 (1964).

⁹² *Id.* at 168, citing United States v. Philadelphia Nat'l Bank, 374 U.S. 321, 343 (1963); cf. United Gas Improvement Co. v. Continental Oil Co., 381 U.S. 392 (1965).

⁹³ 378 U.S. at 173. Note: The district court found the record disclosed "no clue" as to how one parent would have reacted if the other parent had chosen to enter individually. 217 F. Supp. at 130. The phrase "no clue" is unfortunate and can be criticized in that a *possibility* of individual entry by the remaining parent existed, however likely or unlikely.

⁹⁴ 378 U.S. at 175.

⁹⁵ *Id.* "Potential competition cannot be put to a subjective test." *Id.* at 174.

probable in the absence of venture formation.⁹⁶ This approach adds confusion to any meaningful distinction between a possibility-probability delineation. In addition, it raises the basic question of the relative values of actual and potential competition in terms of competitive impact, and a proper separation of the two.

District Court's Remand Decision. Upon remand,⁹⁷ the parties were able to agree on two issues before the district court. The first issue to be determined was whether there was a reasonable probability, but for the formation of Penn-Olin, that *either* parent would have constructed a plant in the Southeast.⁹⁸ If this issue was resolved in favor of the Government, the second issue was: if either parent had entered the Southeast individually, would the other parent have maintained, as a reasonable probability, such continued interest in the Southeastern sodium chlorate market as to make it a significant potential competitor. An adverse ruling for the Government on either issue would require dismissal of the action.

The Government contended that a favorable finding for it on the first two issues would require a conclusion that the venture *probably* had the effect of substantially lessening competition. The defendants contended these findings would present only a *possible* basis for such conclusions, depending upon an evaluation of additional evidence, and that a third issue must be faced.⁹⁹ This issue was "[w]hether the organization of Penn-Olin, as a reasonable probability, resulted in substantially less competition than would have existed if either Olin or Pennsalt had constructed a sodium chlorate plant in the Southeast while the other continued to have an interest in constructing such a plant."¹⁰⁰ This issue was never reached because the court found adversely to the Government on the first issue.

Although the third issue was not considered, it illustrates the proper determination which must be made unless the proper section 7 standard of "substantially lessening competition" is to be ignored. Inherent in any new business venture formation is a new competitive entity in the relevant market. If the venture is successful as in the case of Penn-Olin, competition is thereby increased. If the Government undertakes to attack an increase in competition in its incipiency, it should bear the full burden of proving that this increase, as a matter of reasonable probability, is substantially less than would have occurred but for the venture formation.

As to the first issue, the district court rejected the Supreme Court's suggestion that overall capacity and interest may establish a *prima facie* case of entry, and held that, as a matter of reasonable probability, neither Pennsalt nor Olin would have made independent entry into the Southeastern market in the absence of the joint venture. The Government was held, properly, to a strict standard of proof based upon a preponderance of the evidence and failed to carry the burden. Of particular significance

⁹⁶ Comment, *supra* note 17, at 111.

⁹⁷ *United States v. Penn-Olin Chem. Co.*, 246 F. Supp. 917 (D. Del. 1965).

⁹⁸ *Id.* at 919.

⁹⁹ *Id.*

¹⁰⁰ *Id.*

was that the court reached its conclusion that neither parent would have entered the market only after a penetrating analysis of the motivations of each particular parent.

Upon appeal of this remand decision, the judgment of the district court was affirmed by an equally divided Supreme Court without opinion.¹⁰¹ This second appeal was based on the Government's position that the lower court improperly applied a standard of subjective intent in determining that neither parent would have entered the market independently. The primary contention was that "subjective" evidence concerning what top management thought or said about individual entry was far less probative than "objective" economic evidence based on capacity and incentives for individual entry. It was argued that all evidence on market behavior *after* venture formation had little bearing on the issue of probability of entry. With respect to potential competition, it was urged that entry by one parent would not have deterred interest or entry by the remaining parent because Pittsburgh Plate Glass entered the expanding market after venture formation. The Government's position that a section 7 violation exists if one parent would have entered while the other hovered on the side was also reasserted.¹⁰²

In the response, defendants urged that *Penn-Olin* was distinguishable from every other section 7 case which had been before the Supreme Court because *neither* of the parents had been in the relevant market.¹⁰³ A merger between actual and potential competitors involves some subtraction of competition. But in *Penn-Olin* there was no subtraction; the combination increased competition in the market. With respect to probability of independent entry, defendants acknowledged that the Government did not have to establish actual intent, but reminded the court that "the burden is not on us to establish impossibility of entry but is on the government to establish probability."¹⁰⁴ The further contention was made that probability of entry is solely a question of fact—not an antitrust issue—which should be determined before the antitrust issue of probability of substantial lessening of competition can be treated. In this connection, events occurring after venture formation would have an important bearing in that a new business venture can act only prospectively, while a merger's foreclosure is present.¹⁰⁵

Identifying Potential Competitors—Subjective vs. Objective Standard. The lack of validity of an objective capacity-plus-interest approach as as-

¹⁰¹ Justice Marshall did not participate. *United States v. Penn-Olin Chem. Co.*, 389 U.S. 308 (1967).

¹⁰² ANTITRUST & TRADE REG. REP., No. 335, at A-1 to A-4 (Dec. 12, 1967).

¹⁰³ The main cases relied on by the Government were distinguished as involving quite different circumstances: *FTC v. Procter & Gamble Co.*, 386 U.S. 568 (1967) (only one significant potential competitor for the market); *United States v. Continental Can Co.*, 378 U.S. 441 (1964) (involving both actual and potential competition between two companies); *United States v. El Paso Natural Gas Co.*, 376 U.S. 651 (1964) (involving actual competitors in reality).

¹⁰⁴ ANTITRUST & TRADE REG. REP., No. 335, at A-5 (Dec. 12, 1967).

¹⁰⁵ "The difference, of course, is that the merger's foreclosure is present while the joint venture's is prospective." 378 U.S. at 173-74.

serted by the Government becomes readily apparent when the parents are large diversified corporations. Such companies have numerous arenas of know-how, financing, and manpower, and are generally in quest of expansion via attractive investment opportunities. These companies may, in a general sense, be considered potential competitors in many fields.¹⁰⁶ The practical result of adopting the suggested prima facie approach is to place the entire burden of proof on these venturers to show cause why they should not be divested of their progeny.¹⁰⁷

The district court's analysis of Olin in its second decision provides an excellent example of the decision-making process of a large diversified corporation. Olin was organized into seven separate operating divisions, but all new projects and substantial expenditures required approval on the corporate level. Proposals from each division were in competition for available funds and profit opportunities recommended by other divisions. Once a year each division prepared a report covering a multitude of expenditures and projects deemed advisable to pursue in the next five years. This report was presented to a staff of experts on the corporate level, which met with division personnel before accepting or rejecting each proposal, in whole or in part. If the proposal survived this hurdle, it was passed on to the Capital Appropriations Requirements Committee for further deliberation and ultimate rejection or favorable recommendation to the corporate president. Any project such as Penn-Olin requiring an expenditure over \$25,000 had to go to the Board of Directors with the president's approval before any final decision could be reached.

A determination as to whether Olin was a potential competitor would have been simple had Olin's Board of Directors initially opted to make an independent entry and then later formed a new decision to enter via the venture. Extenuating circumstances other than attempting to avoid competition may cause such a course of action, but it is difficult to imagine a situation more closely approximating *certainty* of potential competition. Since the statute does not require a finding of certainty, a fair solution would be to drop back to the presidential level. Thus, a project recommended to the Board of Directors by Olin's president could be considered as a reasonably probable undertaking. As the district court pointed out, it is "essential to distinguish between the views and actions of those in the Olin organization who were charged with decision-making responsibility, and those whose function it was to make preliminary studies and recommendations. Obviously the former are vastly more significant than those of the latter in predicting *hypothetically* what Olin would have done but

¹⁰⁶ "The courts will be blinding themselves to business reality if it is not recognized that before embarking upon a joint venture each parent will evince an interest in independent entry into the market in question, if it has capacity for such entry." Comment, *supra* note 17, at 113.

¹⁰⁷ It has been suggested that overall capacity by the parents to enter the market individually at a profit should establish a presumption that they "would" have done so but for the venture. The burden of proof would then shift to the parents for rebuttal as they would presumably be in the best position to explain the economies of their decision. Note, *supra* note 18, at 404.

for the joint venture.¹⁰⁸ This approach strikes a workable medium between *certainty*¹⁰⁹ and *possibility*.¹¹⁰

One writer suggests as a test for potential competition a rate of return analysis as reasonably approximating business reality.¹¹¹ This would apply after the Government establishes capacity and interest, and would be based on the particular company's criteria for new investment—especially projected rate of return—as compared with the studies prepared for proposed individual entry. This approach is far superior to the Supreme Court's suggested capacity-plus-interest standard, but still leaves the door open for a multitude of possibilities.

It is proper to assume that the president of a large diversified corporation will not recommend adoption of proposed projects unless that corporation's rate of return requirement is met and the project is within the corporation's corporate debt and capital investment limitations. But the president, being responsible to his board of directors, must satisfy himself that the appraisals upon which he makes his recommendations are accurate and realistic. In addition, the president may choose not to recommend some proposals which satisfy the corporation's rate of return requirement, but are less favorable than others. In essence, the president's recommendation can provide a clear and definite line of demarcation for probable market entry.

Once recommendation is made, the screening task of the president is concluded and the board of directors must decide which of many remaining competing projects appear to be the most favorable. There are and have been countless corporate presidents who readily would agree that there is nothing certain about their recommendations being accepted by their boards.¹¹² Factors for the board's consideration include other recommended undertakings with higher projected rates of return, projects with a lower manpower drain, projects with better consumer contacts,¹¹³ projects with more technological certainty,¹¹⁴ projects requiring less capital investment thus allowing more diversification, and projects facing fewer entry barriers.¹¹⁵

Those astute in the workings of the business world could, no doubt, add dozens of additional considerations which face a board of directors.

¹⁰⁸ 246 F. Supp. at 919 (emphasis added).

¹⁰⁹ Note the court's warning that even if the proposal passed muster with the staff, the Capital Appropriations Requirements Committee, and the president,

no intelligent forecast can be made as to the likelihood of its approval by the Board of Directors who had the final say. . . . The names of at least some of the . . . members mark them as men of broad financial and business experience. Whether these men were hypercritical or easily persuaded to accept management proposals is not disclosed. Their record in approving or disapproving such proposals is not revealed. What their views would have been about a wholly owned chlorate facility which had been a controversial subject for so many years, cannot be conjectured.

Id. at 927-28.

¹¹⁰ Note 80 *supra*.

¹¹¹ Comment, *supra* note 17, at 114.

¹¹² Only two officers of Olin, including the president, had votes on its fifteen-member Board.

¹¹³ Olin had excellent consumer relations in the Southeast, but Pennsalt did not.

¹¹⁴ Olin had never commercially produced sodium chlorate.

¹¹⁵ Hooker and American Potash held a "virtual monopoly" in the Southeast prior to the venture formation.

Limiting the Government's burden of proof to establishing that the proposed project was within that corporation's rate of return criteria does not sufficiently establish reasonable probability. Conduct of an average reasonable corporation should be irrelevant in this prediction of probable consequences. Only by concentrating on the specific company in question can the courts make an intelligent forecast. The factors that make a particular company a potential competitor in a general sense, such as capacity, interest, and reasonable rate of return, do not have controlling significance as to how the particular corporation might have proceeded.¹¹⁶

Potential Competition in Proper Perspective. The Supreme Court in *Penn-Olin* was concerned expressly with the competitive effects of the venture formation, and the case ultimately evolved into the question of foreclosure of potential competition. The effect of elimination of potential competition should approximate removal of actual competition (*i.e.*, removal of a present, identifiable force, increased economic power of market occupants and tendency to create a monopoly).¹¹⁷ When analyzing this foreclosure as a result of a joint venture, the courts will be forced to evaluate an uncertain quality (potential competition) in the context of an uncertain legal standard (incipient threats) in the face of an increase in actual competition.

No meaningful discussion can be had on the trouble and confusion surrounding "potential competition" without recognizing the two different legal uses of the term. Distinction should be made between (1) a condition of freedom of future entry in the relevant market, and (2) a condition of positive competitive force due to the immediate threat of

¹¹⁶ Taking the suggested approach one step further, suppose it can be established as a certainty or reasonable probability that Pennsalt or another competitor planned to enter the market individually. If Olin's staff and president knew of this intention prior to a recommendation to the Board, the recommendation would still be valid toward establishing Olin's probable action. Any earlier studies would be adjusted to take into account the new entrant. Should a certain or probable entrant emerge prior to Board consideration, deliberation would necessarily revolve around this new factor. If the recommendation were rejected outright, Olin could no longer be considered to be "at the edge of the market, continually threatening to enter."

If the proposal were returned for additional study, Olin would still be considered a potential entrant, but additional factors must be considered before a determination of impact in the market place as a potential competitor could be derived. At this point, it would be proper to consider Olin as a significant potential competitor, exerting an influence in the market place, if its established new business rate of return criteria—adjusted for the new or probable entrant—was satisfied.

¹¹⁷ In the *El Paso Natural Gas* merger case, *United States v. El Paso Natural Gas Co.*, 376 U.S. 651 (1964), the Supreme Court ordered divestiture of Pacific Northwest by El Paso. Pacific Northwest was found to have been a substantial factor in the relevant Southern California market even though it had no pipelines into California and had been unsuccessful in its attempts to sell gas there.

The effect on competition in a particular market through acquisition of another company is determined by the nature or extent of that market and by the nearness of the absorbed company to it, that company's eagerness to enter that market, its resourcefulness, and so on. . . . Unsuccessful bidders are no less competitors than the successful one. The presence of two or more suppliers gives buyers a choice. Pacific Northwest was no feeble, failing company; nor was it inexperienced and lacking in resourcefulness. It was one of two major interstate pipelines serving the trans-Rocky Mountain States. . . . It had adequate reserves and managerial skill. It was so strong and militant that it was viewed with concern, and coveted, by El Paso. *Id.* at 660-61. See generally *Aluminum Co. of America v. FTC*, 284 F. 401 (3d Cir. 1922), *cert. denied*, 261 U.S. 616 (1923); *Hale & Hale, Potential Competition Under Section 7: The Supreme Court's Crystal Ball*, 1964 SUP. CT. REV. 171; O'Brien, *Potential Competition Under the Sherman Act Cases*, 12 ABA ANTITRUST SECTION 105 (1958).

new entry by an identified firm.¹¹⁸ The first use of the term is concerned with the opportunities in general for entry by new companies or for expansion of existing companies into a particular relevant market. This use has reference to the traditional "relevant economic factors" analysis which courts undergo in determining the effect of mergers upon actual competition.¹¹⁹ A showing that a venture substantially raises barriers of future entry, thereby reducing potential competition in this general sense, would be but one factor for a court's consideration in determining whether the venture substantially lessens actual competition. The second use of the term refers to the elimination of competition that section 7 was designed to protect, and requires reading the statute to proscribe what "may be substantially to lessen *potential* competition."¹²⁰ Although the Supreme Court did not specifically delineate between these two concepts of potential competition it is reasonable to conclude, for the purposes of *Penn-Olin*, that the Court was concerned with protecting potential competition which exerts a positive competitive impact on the relevant market.¹²¹ The presence of this type of potential competition should not be over-estimated however, as it alone will never supplant the competitive impact of actual competition provided by a venture.

In a joint venture setting, competition in the relevant market is augmented substantially if the venture is successful. In a concentrated industry, the market power of established firms will be diminished, the number of competing firms increased, the relative size and market shares reduced, and the industry's structure one step less oligopolistic. This was the result of the Penn-Olin venture, and should have been considered as cheerful news by all anti-concentration analysts.

In pursuance of the test proposed by the Supreme Court, suppose it is determined that one of the parents would have entered the relevant market, while the other parent remained at the edge threatening entry. The Government's burden of proof, at this point at least, should be to show by a preponderance of the evidence that the increase in competition afforded by the venture may be *substantially* less than the combined market influence of the one parent's entering individually plus the other's market effect as an imminent entrant. While this approach requires (1) assessment of the increase in actual competition afforded by a venture, (2) speculation on the amount of increase in competition which one entering parent would provide, and (3) conjecture on the marketing impact of

¹¹⁸ Rahl, *Applicability of the Clayton Act to Potential Competition*, 12 ABA ANTITRUST SECTION 128, 132 (1958).

¹¹⁹ Includes degree of concentration in an industry, relative size of firms, number of competing firms, prior histories of mergers in the industry, degree of competition between merging firms, and overall behavior of the industry. For excellent discussion in terms of market power, see Dean & Gustus, *Vertical Integration and Section 7*, 40 N.Y.U.L. REV. 672 (1965).

¹²⁰ In merger cases, potential competition sought to be protected should possess "positive substantial competitive force of such degree as to rank with actual competition and further . . . [be] great enough in and of itself to qualify for statutory protection." Rahl, *supra* note 118, at 133.

¹²¹ "The existence of an aggressive well equipped and well financed corporation engaged in the same or related lines of commerce waiting anxiously to enter an oligopolistic market would be a substantial incentive to competition which cannot be underestimated." 378 U.S. at 174.

the waiting non-entering parent, it is the only proper avenue to reach the statutory standard.

Another essential requirement in a proper burden of proof should be the identification of the firm or firms exerting the competitive influence sought to be protected. In venture cases this normally would be one parent or the other. But the contention can also be made that the joint venture may foreclose entry by other non-parent competitors. In this situation, the Government should be compelled to identify the particular potential competitor source sought to be protected, and to show how this force substituted for or supplemented actual competition so that its removal after the venture's entry substantially would lessen overall competition in the relevant market as a matter of reasonable probability. This proof should show that conditions of entry were good for this particular potential competitor; otherwise its threat of entry could not exert an important force on the relevant market. Thus, the Government must prove a factual background substantially the opposite of that which it must prove in a regular section 7 merger case involving a foreclosure of actual competition, where prosecutors normally attempt to establish high entry barriers.

Attempts to balance the benefits of increased actual competition against the loss of potential competition only point to the basic weakness of emphasizing potential competition in a joint venture setting. As illustrated above, it is difficult to identify who may be potential entrants in a particular market. Changes in management goals, technology, and economic conditions can alter quite suddenly the status of would-be entrants.¹²² Venture formation may or may not deter would-be entrants,¹²³ whose presence and effect should be determined and accumulated with the effect of foreclosure of potential competition of the parent that would have remained at the market's edge but for the venture. If other potential competitors remain at the market's edge after venture formation, any void created by the loss of potential competition from a would-be remaining parent is substantially filled. A determination should also be made as to what effect individual entry by one parent would have had on the anxiousness of the remaining parent. Loss of interest by this parent may or may not have any effect upon other expanding companies.

From the standpoint of judicial administration, it seems very desirable to de-emphasize the importance of potential competition as much as possible in joint venture cases, except in the most obvious situations. Tests for determining the identity of potential entrants, whether in terms of internal corporate intent as suggested herein or in terms of capacity-plus-interest as pressed by the Government, "tend to mire antitrust proceedings in a prolonged and unsatisfactory examination of what corporate officials either intended as to themselves or understood regarding others."¹²⁴ Attempts to prove the probable effect of an identified potential entrant must

¹²² Backman, *supra* note 10, at 669-70.

¹²³ Pittsburgh Plate Glass entered the relevant market subsequent to Penn-Olin's formation, 217 F. Supp. at 127.

¹²⁴ Brodley, *Oligopoly Power Under the Sherman and Clayton Acts—From Economic Theory to Legal Policy*, 19 STAN. L. REV. 285, 332 (1967).

yield largely unsuccessful results and involve a considerable waste of time and energy.

When the Government undertakes divestment of the venturers' progeny, it should be required to sustain its full burden of showing reasonable probability.¹²⁵ Proof of capacity and interest merely lays a foundation for proof of reasonable probability. Never to be lost in the maze of speculation inherent in the determination of potential competition is the fact that a joint venture does exert present, actual competition in its relevant market. The Government's burden should only be discharged if it can demonstrate that another set of circumstances, which would have occurred as a matter of reasonable probability, would have increased competition more than venture formation. While this position will seem unduly harsh to some, it must be remembered that incipient threats to potential future competition are the subjects of the Government's attacks. This circumstance, in view of an increase in actual competition, mitigates what might otherwise be an undue burden of proof for the Government.

IV. PROPRIETY OF APPLYING SECTION 7 TO NEW BUSINESS JOINT VENTURES

Legislative History and Suggested Statutory Construction. In *Penn-Olin* the Supreme Court was confronted with applicability of section 7 of the Clayton Act to new business joint ventures for the first time. The original enactment of 1914 was prompted by judicial hesitancy to apply the Sherman Act with the stringency which Congress desired, and was also directed toward abuses of holding companies that acquired *stock* in previously independent corporations as a device to control or eliminate competition among them.¹²⁶ It was designed specifically to cope with incipient threats to competition before they reached Sherman Act proportions.¹²⁷

The 1950 amendment was designed to plug the *assets* loophole which existed in the original Act¹²⁸ by preventing "corporations from acquiring another corporation by means of acquisition of its assets, where under the present law it is prohibited from acquiring the stock of said corporation."¹²⁹ The legislative histories of the original enactment and the 1950 amendment contain no references relating to new business joint venture

¹²⁵ "We think it is plain that before a merger may be condemned merely because its effect may be to lessen *potential* competition it must be ascertained that the potential competition is a reality, that is to say, that there is a reasonable probability of such potential competition." *United States v. Crocker-Anglo Nat'l Bank*, 223 F. Supp. 849, 855-56 (N.D. Cal. 1963).

¹²⁶ H.R. REP. NO. 627, 63d Cong., 2d Sess. at 2 (1914); S. REP. NO. 698, 63d Cong., 2d Sess. at 1 (1914). The second paragraph of original section 7 was designed to reach holding companies. "No corporation shall acquire, directly or indirectly, the whole or any part of the stock or other share capital of two or more corporations engaged in commerce where the effect of such acquisition, or the use of such stock by the voting or granting of proxies or otherwise, may be to substantially lessen competition between such corporations, or restrain such commerce in any section or community, or tend to create a monopoly of any line of commerce." 38 Stat. 731 (1914).

¹²⁷ D. MARTIN, *MERGERS AND THE CLAYTON ACT* 46 (1959); Votaw, *Antitrust in 1914: The Climate of Opinion*, 24 ABA ANTITRUST SECTION 14 (1964).

¹²⁸ 96 CONG. REC. 16450 (1950); McAllister, *Where the Effect May Be To Substantially Lessen Competition or Tend To Create a Monopoly*, 3 ABA ANTITRUST SECTION 124, 139-45 (1953).

¹²⁹ S. REP. NO. 1775, 81st Cong., 2d Sess. at 2 (1950).

coverage.¹³⁰ The Supreme Court in *Penn-Olin*, however, based its decision on the amendment to section 7.

The prohibitions contained in amended section 7 basically cover direct or indirect acquisition by a corporation engaged in interstate commerce of all or part of the stock or assets of another corporation "engaged also in commerce." The defendants argued that Penn-Olin was not "engaged also in commerce" at the time of its formation and stock issuance to the parents, and therefore was not reached by section 7. The Government argued that an entity comes within the meaning of section 7 if, at the time of the challenged acquisition, it is either conducting an interstate business or is intending or preparing to do so.¹³¹ The Supreme Court did not adopt either of the above arguments, but nevertheless held section 7 applicable.

The Court employed a rather dubious course of reasoning to reach applicability of this anti-merger statute designed to deal with corporate extinctions. It held that the test of applicability of the section is the effect of the acquisition, and that competition between the *parents* who are engaged in commerce, and the venture would be substantially lessened, if not foreclosed.¹³² While this broad statement is not necessarily true, it completely ignores the basic statutory prerequisite that the acquired corporation be engaged in commerce prior to acquisition before there can be a foreclosure under the terms of the statute. The Court found, however, that "this logic fails in the light of the wording of the section and its legislative background;"¹³³ no serious attempt to explain or expound on either basis was made.

Less alarming was the Court's re-affirmation that competitive effects of an acquisition are measured from the time of suit rather than from the time of acquisition.¹³⁴ This judicial tool is necessary for proper determination in many merger cases, and is even more so in dealing with a new entity unless substantial lessening of competition is to be based on conjec-

¹³⁰ "Examination of the committee reports and floor debate in both houses of Congress yields no suggestion that the 1950 amendment included an effort to extend the law to joint ventures, by 1950 a subject of such grave implications as to have merited extensive committee consideration and floor debate." Flittie, *Status of Joint Venturing Business Combinations Short of Actual Merger Under the Antitrust Laws*, FOURTEENTH INSTITUTE ON OIL AND GAS LAW AND TAXATION 313, 340 (S.W. Legal Foundation 1963); Handler & Robinson, *A Decade of Administration of the Celler-Kefauver Anti-Merger Act*, 61 COLUM. L. REV. 629, 652-74 (1961).

¹³¹ Congress plainly did not intend an acquisition of a company, which was conceived and intended as an interstate firm, to escape the ban of Section 7 merely because, at the moment of acquisition the company itself had not yet produced or shipped any of its own goods. On the contrary, . . . the limitation of Section 7 to acquisitions of stock or assets of corporations 'engaged . . . in (interstate) commerce' reflects only the Congressional intent that the section would not prevent corporations engaged in interstate commerce from acquiring wholly intrastate firms.

Brief for the United States at 30, *United States v. Penn-Olin Chem. Co.*, 378 U.S. 158 (1964).

¹³² "Moreover, in this case the progeny was organized to further the business of its parents, already in commerce, and the fact that it was organized specifically to engage in commerce should bring it within the coverage of § 7." 378 U.S. at 168. Prior to Supreme Court consideration, one writer expressed the view that: "To afford immunity to an acquisition which may have all the effects of a merger simply because it is accomplished indirectly by the formation of a joint company is to promote form at the expense of substance." Note, *Joint Ventures and Section 7 of the Clayton Act*, 14 STAN. L. REV. 777, 780 (1962).

¹³³ 378 U.S. at 168.

¹³⁴ *Id.*, citing *United States v. E.I. du Pont de Nemours & Co.*, 353 U.S. 586, 607 (1957).

ture in all but the most obvious cases. This dilemma illustrates the difficulty inherent in attempting to predict future consequences of a new market entrant by a reasonable probability standard. Thus, the Court's attempt to pass off the "engaged in commerce" requirement as a technicality actually demonstrated a basic weakness in applying section 7 to new business joint ventures.

The Supreme Court clearly chose applicability on the basis of what they thought antitrust policy *should* be. The Court was fearful of allowing a "joint venture loophole" and considered joint ventures a form of "quasi merger."¹³⁵ In addition, it was the majority's view that joint ventures should be subject to an incipiency standard as a matter of policy. This concern for an incipiency standard relates to the Court's preoccupation with potential competition and does not provide a compelling policy reason for applying section 7. Only three years after passage of the Sherman Act it was held that neither the letter of that law nor its purpose "distinguishes between strangling a commerce which has been born and preventing the birth of a commerce which does not exist."¹³⁶ Furthermore, in emphasizing protection of public interest under the Sherman Act, Judge Learned Hand stated "it can make no difference whether an existing competition is put an end to, or whether prospective competition is prevented."¹³⁷

The *Penn-Olin* Court refused to become involved in exhaustive scrutiny of the original enactment, the 1950 amendment, or the legislative history of either. Rather, the majority brushed under its judicial rug the far reaching consequences of applicability of section 7 to new business joint ventures, stating that "we are but expounding a national policy enunciated by the Congress to preserve and promote a free competitive economy."¹³⁸ This national policy was found in Congress' extension of original section 7 to cover asset acquisitions of going concerns.

While *Penn-Olin* is not novel as an example of judicial legislation, it does provide another example of the Supreme Court's proclivity to expand its influence beyond the traditional bounds of the checks and balances system. The Department of Justice and the Federal Trade Commission were never able to attack successfully an asset acquisition prior to the 1950 amendment and conceded inapplicability of original section 7.¹³⁹ In 1950, while strenuous efforts were being made to enact the Celler-

¹³⁵ 378 U.S. at 168, citing *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321, 343 (1963); cf. *United Gas Improvement Co. v. Continental Oil Co.*, 381 U.S. 392 (1965).

¹³⁶ *United States v. Patterson*, 59 F. 280, 283 (C.C.D. Mass. 1893), endorsed by the Supreme Court in *United States v. United Shoe Mach. Co.*, 247 U.S. 32, 58 (1918).

¹³⁷ *United States v. Aluminum Co. of America*, 148 F.2d 416, 429 (2d Cir. 1945). See also *United States v. Paramount Pictures, Inc.*, 334 U.S. 131, 150-53 (1948); *United States v. Griffith*, 334 U.S. 100, 107 (1948); *United States v. Reading Co.*, 226 U.S. 324, 351, 369-71 (1912).

¹³⁸ 378 U.S. at 170. In further attempting to justify its judicial extension, the Supreme Court mentioned the "grand design of the original § 7 . . . to arrest incipient threats to competition which the Sherman Act did not ordinarily reach . . ." *Id.* at 170-71. In *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321 (1963), the Court concluded that the purpose of the 1950 amendment was to broaden section 7 to cover "the entire range of corporate amalgamations." *Id.* at 342.

¹³⁹ *Arrow-Hart & Hegeman Elec. Co. v. FTC*, 291 U.S. 587 (1934); 33 OP. ATT'Y GEN. 225, 241 (1922); 1 F.T.C. 541-42 (1919).

Kefauver amendment, the Department of Justice attempted to cure the "assets loophole" before a district court that was sympathetic to its goal.¹⁴⁰ Nevertheless, the court accepted the proper balance between the legislative and judicial branches and refused to amend section 7 by judicial legislation.

Application of a provision in original section 7 which was not altered by the 1950 amendment was urged in *Penn-Olin*. This paragraph (paragraph 3) provides:

Nor shall anything contained in this section prevent a corporation engaged in commerce from *causing the formation* of subsidiary corporations for the actual carrying on of their immediate lawful business, or the natural and legitimate branches or extensions thereof, or from owning and holding *all or a part* of the stock of such subsidiary corporations, *when the effect of such formation is not to substantially lessen competition.*¹⁴¹

The contention was made that Penn-Olin was a subsidiary of both Pennsalt and Olin, and therefore entitled to consideration under this paragraph. Although paragraph 3 has never been ruled on, the trial court merely noted the contention and the Supreme Court ignored it. It is most unfortunate that a careful analysis of paragraph 3 was not made, as it provides an excellent avenue for reconciling joint ventures under section 7. *Penn-Olin* was decided under the "may be" or "reasonable probability" standard while under paragraph 3, the Government would have had to prove that the venture's effect *was* to lessen substantially competition. The effect of such a holding, in essence, would be a welcomed recognition that the Sherman Act standards were intended to test anticompetitive effects of new business. This conclusion would be sound, for although the Clayton Act supplements the Sherman Act, it was designed and intended to deal with corporate *extinctions* and the stifling of competition by holding companies acquiring stock in *existing* corporations. Moreover, the courts would be relieved of drawing many of the difficult distinctions previously pointed out herein.

The Government contended that since paragraph 3 speaks of "a corporation" causing subsidiaries to be formed, it cannot be applicable to a situation where two or more corporations create a single subsidiary.¹⁴² It was also contended that joint companies are not "subsidiaries" as used in paragraph 3 and that congressional debates preceding passage of the 1914 enactment make it clear that the intent was to permit chain or branch stores to be formed by a single parent corporation.¹⁴³

Since paragraph 3 does not provide an interpretation of what "a part

¹⁴⁰ *United States v. Celanese Corp. of America*, 91 F. Supp. 14 (S.D.N.Y. 1950). "This Court cannot amend Section 7 by judicial legislation The instrumentality to combat this evil which the Government says is a threat to a well-balanced, free, competitive economy, must come from Congress." *Id.* at 17.

¹⁴¹ 38 Stat. 731 (1914), 15 U.S.C. § 18 (1964) (emphasis added).

¹⁴² Post Trial Brief of the United States at 34, *United States v. Penn-Olin Chem. Co.*, 217 F. Supp. 110 (D. Del. 1963).

¹⁴³ *Id.* See also 51 CONG. REC. 9073, 14314-15 (1914). "The essence of subsidiary status which distinguishes it from all other ownership interests in a corporation is single control by a single parent." Post Trial Brief of the United States at 35, *United States v. Penn-Olin Chem. Co.*, 217 F. Supp. 110 (D. Del. 1963).

of the stock" means, the Government set out its interpretation, which could be of great importance for future joint venturers.

Section 7's main purpose was not to inhibit the normal processes of internal growth by individual corporations, whether by creation of new plants, new divisions or new wholly owned subsidiaries. The third paragraph, however, speaks of the forming of subsidiaries by 'a corporation' which thereafter holds 'all or a part of the stock.' To the extent that a part of the stock is held by others (up to 49% of the total), questions of joint ownership and external combination require an examination of competitive effects. In such a case the statute imposes the burden on the controlling shareholder to show that the creation's effect 'is not' to lessen competition substantially. Satisfying this test, i.e., of no *present* anticompetitive effect, would enable the majority stockholder of a subsidiary to avert suit under the earlier paragraphs of Section 7 in which its burden would otherwise be to refute a charge that anticompetitive effects will probably occur in the *future*, i.e., where 'the effect . . . may be substantially to lessen competition.'¹⁴⁴

Thus, it is the Government's position that as long as one venture parent owns as much as fifty-one per cent of the stock, the venture will not be tested under a reasonable probability standard.¹⁴⁵

Not to go unnoticed is the Government's contention that the majority stockholding parent would have the burden of proving that the venture *does not* substantially lessen competition. While this is a matter of statutory construction, it is submitted that once the majority stockholder establishes fifty-one per cent ownership, the burden should shift to the Government to show substantial existing anticompetitive effects. This paragraph should be construed as an acknowledgment by Congress of the necessity for and the benefits that can be derived from new internal or joint growth, and not as a special restrictive exemption.

It is most improbable that in 1914 Congress intended to deal with sophisticated concepts of subsidiary, affiliate, or joint venture. The Government can cite no references to congressional intent that fifty-one per cent ownership be of special significance. Instead of second-guessing as to what Congress meant by "subsidiary" in 1914, paragraph 3 should be construed as a policy statement by Congress of its intent that new business enterprises not be strangled in their inception by the Clayton Act.

The congressional purpose for enacting paragraph 2 of the Clayton Act was to facilitate attacks against holding companies that were strangling competition by acquiring stock in existing competitors.¹⁴⁶ One of the purposes for enactment of paragraph 3 of the Clayton Act was to permit establishment of chain or branch stores in subsidiary form which by their very nature would be new competitive entities. But most significantly, Congress did *not* limit paragraph 3 to chain or branch stores

¹⁴⁴ *Id.* at 36.

¹⁴⁵ The Government draws some support for this from the *Pan American* case, which, ironically, supports the adequacy of the Sherman Act in coping with anticompetitive ventures. "Panagra is not a subsidiary of Pan American; . . . If Pan American were the majority shareholder in Panagra or if Panagra were a wholly owned subsidiary of Pan American it might make a decisive difference in this case." *United States v. Pan Am. World Airways, Inc.*, 193 F. Supp. 18, 40 (S.D.N.Y. 1961)

¹⁴⁶ *Supra* note 126.

or ownership by a single parent corporation. It is submitted that Congress intended that new competitive entities not be subject to the same anticompetitive standards as paragraphs 1 and 2 which were designed to deal with corporate extinctions and holding companies.

Congressional debate¹⁴⁷ in 1914 and a fair reading of the language of section 7 indicate that Congress intended to make all stock acquisitions, whether in established companies or new entities and whether complete or partial, subject to a section 7 test. If the Clayton Act must be applied to new business joint ventures, both antitrust policy goals and the American system of free enterprise will be better served by testing their competitive effects under the subsidiary paragraph (paragraph 3) of section 7. To do otherwise may all too often inhibit the creation of challenging new competitors in a relevant market and thereby perpetuate and protect existing competitors.

Future Trials and Tribulations. Prerequisite to measuring the competitive effects of joint ventures will be ascertainment of the line or lines of commerce and the section or sections of the country involved. The statutory phrase "any line of commerce in any section of the country" divides the relevant market into product and geographic categories, and modifies both tests of illegality contained in section 7—substantial lessening of competition and tendency to create a monopoly.¹⁴⁸ Both product and geographical boundaries are generally measured with regard to "area of effective competition,"¹⁴⁹ and the Government has some burden of proof in these determinations.

With respect to line of commerce or product market, a variety of criteria must be dealt with. Ventures must now run the gauntlet between the standard economic concept of cross-elasticity of demand¹⁵⁰ and the concept of product submarkets within product markets.¹⁵¹ When a venture's new product does not fit into a product market by conventional economic standards, courts might look to inter-industry and potential competition from other products and submarkets therein to measure competitive effects.¹⁵² With respect to relevant geographic markets, venture products normally will be sold in areas of less than nationwide scope, which can lead to extremely difficult problems of predictable delineation. It is easy to state that the quest for a relevant geographic market is to be

¹⁴⁷ 51 CONG. REC. 14468-72 (1914); see *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321, 335-49 (1963).

¹⁴⁸ S. REP. NO. 1775, 81st Cong., 2d Sess. at 8 (1950). These tests do not apply to pure conglomerate joint ventures.

¹⁴⁹ The "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." *Tampa Elec. Co. v. Nashville Coal Co.*, 365 U.S. 320, 327 (1961).

¹⁵⁰ In terms of a product market extending to the point where there is low interchangeability between the product and substitute products. See *Brown Shoe v. United States*, 370 U.S. 294, 325 (1962); cf. *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 393-404 (1956).

¹⁵¹ *Brown Shoe v. United States*, 370 U.S. 294, 325 (1962). Anticompetitive effects in a submarket can be fatal. *United States v. Aluminum Co. of America*, 377 U.S. 271, 277 (1964). Among factors used to establish submarkets are: (a) industry or public recognition of submarket as distinct from overall market for products, (b) peculiar characteristics and uses, (c) unique production facilities, (d) distinct customers, vendors or prices, and (e) sensitivity to price changes.

¹⁵² *United States v. Continental Can Co.*, 378 U.S. 441, 452-58 (1964).

approached in a pragmatic, factual manner rather than a formal, legalistic one, and that it must " 'correspond to the commercial realities' of the industry and be economically significant."¹⁵³ It is quite another matter to cope with geographic submarkets and different geographic markets at different levels of distribution.¹⁵⁴

In short, geographic and product markets have not been refined to any consistent principles for confident predictability. As stated by one commentator:

Because of the relative flexibility with which the Court has dealt with the problem of market boundaries, the term 'relevant market' for Clayton 7 purposes does not, and cannot refer to a 'market' in any single economic or trade sense, but refers rather to a product-geographic locale where third companies (competitors, suppliers, or customers) may be affected by an acquisition—and nothing more.¹⁵⁵

The task of counsel will be to anticipate *all* significant areas where particular competitors, suppliers, or customers *may* be affected by venture formation before "star-gazing" can begin on the crucial question of prospective *probability* of substantial lessening of competition. The following general criteria for assessing the probability of a substantial lessening of competition were given by the Supreme Court:

[T]he number and power of the competitors in the relevant market; the background of their growth; the power of the joint venturers; the relationship of their lines of commerce; the competition existing between them and the power of each in dealing with the competitors of the other; the setting in which the joint venture was created; the reasons and necessities for its existence; the joint venture's line of commerce and the relationship thereof to that of its parents; the adaptability of its line of commerce to non-competitive practices; the potential power of the joint venture in the relevant market; an appraisal of what the competition in the relevant market would have been if one of the joint venturers had entered it alone . . . ; the effect, in the event of this occurrence, of the other joint venturer's potential competition; and such other factors as might indicate potential risk to competition in the relevant market.¹⁵⁶

These factors for testing under section 7 are in addition to specific intent to eliminate competition and specific collateral restrictive agreements between venture parents.

¹⁵³ *Brown Shoe v. United States*, 370 U.S. 294, 336-37 (1962).

¹⁵⁴ *Id.* at 328, 336. As the Supreme Court stated in the *Pabst* case:

Certainly the failure of the Government to prove by an army of expert witnesses what constitutes a relevant 'economic' or 'geographic' market is not an adequate ground on which to dismiss a § 7 case. Compare *United States v. Continental Can Co.*, 378 U.S. 441, 458. Congress did not seem to be troubled about the exact spot where competition might be lessened; it simply intended to outlaw mergers which threatened competition in any or all parts of the country. Proof of the section of the country where the anticompetitive effect exists is entirely subsidiary to the crucial question in this and every § 7 case which is whether a merger may substantially lessen competition anywhere in the United States.

United States v. Pabst Brewing Co., 384 U.S. 546, 549-50 (1966).

¹⁵⁵ B. BOCK, *MARKETS AND MERGERS* 59 (4th ed. 1965). Note the characterization of relevant market in the dissent of Justice Fortas as "this strange red-haired, bearded, one eyed man-with-a-limp classification." *United States v. Grinnell Corp.*, 384 U.S. 563, 591 (1966).

¹⁵⁶ 378 U.S. at 177. The new Merger Guidelines announced by the Department of Justice on May 30, 1968, entitled, "Enforcement Policy for Sec. 7, Clayton Act" contain no reference to joint ventures.

No indication is given regarding the relative importance of the criteria, and it is apparent that many are shades and gradations of others. It is clear, however, that the court is interested in probabilities and not tangible present restraints. The underlying theme centers on foreclosure of potential competition in the relevant market plus opportunities for abuse in related markets.

In the traditional merger case, courts have relied heavily on respective shares of the market of the *acquired and acquiring* companies, their combined share, their respective rankings in the industry with regard to assets and sales, and their combined rank with respect to remaining competitors. If a new business venture is attacked in its incipiency, this information would not be available because competition is being created where none existed before. Nevertheless, evidence of market rankings and percentages of sales, production, and capacity of the venture's competitors in the relevant market can be related to the necessity for venture formation. Since the venture does not combine anything previously existing, a harder look at the number of acquisitions in the corporate growth patterns of the parent corporations, including any previous antitrust violations, can be expected.

Power of the parents and potential power of the venture in the relevant market are closely related. Careful examination will be made of the power of the parents through their creation to drive out small existing competitors or to restrict further entry into the relevant market. This relates to foreclosure of potential competition and barriers to market entry as part of a relevant economic factors analysis. Lack of concentration and a large number of competing units would indicate that entry barriers are few, thus pointing to less justification for entry by joint participation, and vice versa. Joint ventures can be desirable, however, even in non-concentrated markets. In oligopolistic markets, they should be encouraged as a method for reducing existing concentrations.

With respect to driving out existing competitors, inquiry will be made into whether the financial resources of one or more of the parents are such that the venture ultimately could dominate the market, *i.e.*, provide too much competition. In the leading case on anticompetitive "deep pockets,"¹⁵⁷ the Supreme Court upheld a Federal Trade Commission order requiring Procter & Gamble to divest its wholly conglomerate acquisition of Clorox. The Government attacked Procter & Gamble's position as the largest advertiser in the United States and its ability to acquire advertising discounts and shelf space not available to competitors. In addition, the merger would have eliminated Procter & Gamble as a potential competitor in the bleach business, which prior to the merger presumably restrained Clorox from exploiting its position of holding fifty per cent of the market.

Other sources of "potential" power which may be urged are control of an inordinate share of vital raw materials and erosion of tradi-

¹⁵⁷ *FTC v. Procter & Gamble Co.*, 386 U.S. 568 (1967).

tional industry structures through vertical integration, *i.e.*, too much efficiency through economies of scale. If an economic imbalance resulting from parenthood is so great that venture competitors are unable to defend themselves by innovation, increased commitments, etc., this should be a very important factor.

The adaptability of the venture's line of commerce also is related closely to the power of the parents. Opportunities for reciprocity may exist based upon the proposition that the parents, by reason of their size, can use their combined buying power as a basis for making reciprocal arrangements with vendors who are also buyers of the venturer's product from others, thus giving the venture an undue sales advantage.¹⁵⁸ A single parent likewise could become the perpetrator of an illegal tying arrangement, because of its control over the tying products (its substantial purchases), to generate leverage over the tied product (the venture's product sought to be sold).¹⁵⁹

There can be no doubt that reciprocal arrangements which ignore price, quality, and service and substitute coercion in the form of direct or implied threats of economic retribution are illegal.¹⁶⁰ But with joint ventures attacked in their incipiency, courts do not have established reciprocal relationships with which to deal. Since section 7 does not require a showing of certainty, a Government allegation that accumulation of purchasing power by venture formation threatens substantially to lessen competition presumably would rest on the following intermediate propositions: (1) The venture *probably* will generate reciprocal purchasing power for the parents; (2) such power, if generated, *probably* will be used; (3) such power, if generated and used, *probably* will result in foreclosing competition to a substantial share of the relevant market. Proof of these propositions should go well beyond establishing mere *opportunities* (possibility) for abuse. To do otherwise would be to ignore the statutory standard. This quandary of establishing proper proof, similar to dealing with potential lessening of potential competition, further demonstrates the clumsiness of applying paragraph 1 of amended section 7 to joint ventures.¹⁶¹

¹⁵⁸ It is not overly speculative to assume that the judicious use of its steel-purchasing power by Ingersoll-Rand could immeasurably increase the sales by the acquired companies of machinery and equipment to the coal mining companies which acutely need the continued goodwill of the steel industry. Moreover, the mere existence of this purchasing power might make its conscious employment towards this end unnecessary; the possession of the power is frequently sufficient, as sophisticated business men are quick to see the advantages in securing the goodwill of the possessor.

United States v. Ingersoll-Rand Co., 218 F. Supp. 530, 552 (W.D. Pa.), *aff'd*, 320 F.2d 509 (3d Cir. 1963). See also Hale & Hale, *Reciprocity Under the Antitrust Laws; A Comment*, 113 U. PA. L. REV. 69 (1964); Handler, *supra* note 17; Krash, *The Legality of Reciprocity Under Section 7 of the Clayton Act*, 9 ANTITRUST BULL. 93 (1964); Turner, *Conglomerate Mergers and Section 7 of the Clayton Act*, 78 HARV. L. REV. 1313, 1386-93 (1965).

¹⁵⁹ FTC v. Consolidated Foods Corp., 380 U.S. 592 (1965); Northern Pac. Ry. v. United States, 356 U.S. 1 (1958); see Asper, *Reciprocity, Purchasing Power and Competition*, 48 MINN. L. REV. 523, 539 (1964); Comment, *Reciprocal Dealing and the Antitrust Laws*, 77 HARV. L. REV. 873 (1964).

¹⁶⁰ FTC v. Consolidated Foods Corp., 380 U.S. 592 (1965); United States v. General Dynamics Corp., 258 F. Supp. 36 (S.D.N.Y. 1966); United States v. Ingersoll-Rand Co., 218 F. Supp. 530 (W.D. Pa.), *aff'd*, 320 F.2d 509 (3d Cir. 1963); California Packing Corp., 25 F.T.C. 379 (1937); Waugh Equip. Co., 15 F.T.C. 232 (1931).

¹⁶¹ Like almost any other competitive power, purchasing power may be abused. When it is, abuse should be corrected. But violations of law that must be postulated upon

It is submitted that probabilities for reciprocity should be a minor consideration with respect to the validity of a venture. In *United States v. General Tire & Rubber Co.*¹⁶² the Government attacked reciprocity for the first time in the absence of a merger or acquisition. While this case is of utmost importance from the standpoint of possible stringent reciprocity prohibitions in the future, it also demonstrates that restraints ancillary to venture formation do not necessarily require venture dissolution. Certainly, giving any significant weight to mere opportunity for abuse would be as unconscionable as exalting possibility of foreclosure of potential competition.

The relationship of the parents' lines of commerce, the competition existing between the parents, the power of each in dealing with competitors of the other, and the venture's line of commerce in relation to the parents' products are closely interrelated testing criteria. Essentially, courts will be called upon to determine what probable effect participation in the venture will have on future relations of the parents. It will be urged that the closer the relationship of the parents' respective lines of commerce, the more likely there will be horizontal and vertical foreclosures of competition between the parents. If cooperation in the venture is a significant part of the business of otherwise competing parents, the venture will be attacked on the basis that such cooperation will lead to or dictate cooperation in other areas.¹⁶³ While these results do not necessarily follow, feverish "flag waving" by the Government can be expected.¹⁶⁴ Courts will again be mired in probability predictions where opportunities and possibilities will not reach the statutory standard.

Examination of the setting in which the venture was created will require analysis of the market structure and negotiations and arrangements between the parents prior to joint entry. Determinations will have to be made as to whether the industry is oligopolistic with high entry barriers or whether small businesses might be endangered by joint entry. Any pre-incorporation agreements between the parents relating to marketing arrangements, territorial plans, or product pricing will be carefully scrutinized for Sherman Act violations.

The reasons and necessities for venture formation will be critical for the survival of the offspring. A demonstration of increase in actual competition should not be relied on as showing sufficient justification. In addition, the parents should be prepared to give convincing evidence of purposes such as sharing financial burdens which a single parent would not or could not undertake, assuring a source of supply of critical raw materials, utilizing complementary technology and research facilities, or

'probabilities' are hard enough to handle. If we add violations built upon 'opportunities for abuse' and 'probabilities of opportunity for abuse,' two results follow: It is increasingly difficult for one to know what he must do to comply with the law, and the power of enforcement agencies to rearrange rather than merely to correct is 'probably' greatly enlarged.

Asper, *supra* note 159, at 555.

¹⁶² Civil No. 67-155 (N.D. Ohio, filed March 2, 1967).

¹⁶³ *United States v. Minnesota Mining & Mfg. Co.*, 92 F. Supp. 947, 963 (D. Mass. 1950); Comment, *supra* note 17, at 108.

¹⁶⁴ See Justice Douglas' dissent, 378 U.S. at 177.

achieving economies of scale necessary to compete in the relevant market larger than the capacity of either individual parent. All studies and surveys relating to the need for joint formation should be carefully documented and preserved.¹⁶⁵

It is apparent that this array of criteria, along with others previously discussed, will require careful and proper planning from origination through implementation. As soon as possible, the venture should become and be conducted as a separate entity having its own staff of employees and management personnel. Parents should avoid any behavior which could be interpreted as an agreement to avoid competition between each other and preferably with the venture. Ideally, the parents should treat the venture as a stock purchase investment with future negotiations conducted at arm's length.¹⁶⁶

It is evident that these guidelines require examination of all possible anticompetitive effects resulting from venture formation with special emphasis on foreclosures between the parents, the parents and the venture, and the customers and suppliers of the parents. These factors should be tested, but the significance of the guidelines is in what is *omitted*, i.e., the effect of increase in *actual* competition. The fact that joint ventures provide a new competitive force requiring some alteration of the controlling criteria in merger cases was acknowledged by the Supreme Court in *Penn-Olin*, but no perceptible degree of its importance can be surmised.

Increase in actual competition in a realistically structured relevant market should head the list of importance and be balanced against properly proven foreclosures. The overriding public interest should be directed toward improvement of competition and preservation of business experimentation. Only when the Government can demonstrate that a different set of circumstances probably would have produced a greater increase in competition should it prevail under section 7. Even when a venture is unsuccessful and does not measurably increase competition, it should not be condemned unless a substantial lessening is proven as a matter of reasonable probability. In keeping with the substantial lessening standard, the underlying philosophy should be to insure that actual and prospective competition in the relevant market have not been impaired substantially, and that related markets basically are unaffected. An unsuccessful venture may indicate that a larger, more efficient combination of resources is necessary to crack an existing market. In short, if section 7 must be

¹⁶⁵ If merger rationale is extended to joint ventures in this area, parents should not expect a warm reception for their business justifications. Defenses based upon increased efficiency and economies of scale were rejected in *American Tobacco Co. v. United States*, 328 U.S. 781, 813 (1946); *United States v. Aluminum Co. of America*, 148 F.2d 416, 427 (2d Cir. 1945); *United States v. United Shoe Mach. Corp.*, 110 F. Supp. 295, 345 (D. Mass. 1953), *aff'd per curiam*, 347 U.S. 521 (1954). Attempts to justify mergers on the grounds that expansion was necessary to satisfy market demand in a new area, see *United States v. Bethlehem Steel Corp.*, 168 F. Supp. 576, 615-18 (S.D.N.Y. 1958), and that consolidation was necessary to effectively challenge a market leader, see *American Crystal Sugar Co. v. Cuban-American Sugar Co.*, 152 F. Supp. 387, 399 (S.D.N.Y. 1957), *aff'd*, 259 F.2d 524 (2d Cir. 1958), also have not prevailed. See Comment, "Substantially To Lessen Competition . . .": *Current Problems of Horizontal Mergers*, 68 *YALE L.J.* 1627, 1654-62 (1959).

¹⁶⁶ For discussion of drafting problems, see generally Note, *Joint Venture Corporations: Drafting the Corporate Papers*, 78 *HARV. L. REV.* 393 (1964).

applied in new business joint venture cases, the emphasis should be on increases in competition rather than the traditional merger approach of seeking out foreclosures resulting from corporate extinctions.

A rare possibility is that a particular venture was formed merely to avoid competition among the parents. It has been demonstrated herein that the Sherman Act is more than adequate in dealing with such a situation. It is submitted, moreover, that the overriding policy objective should be to stimulate the economy with actual competition by *some* new entry. The fact that amended section 7 is not designed to cope with incipient threats posed by *new entrants* should in no way lighten the Government's task. Having chosen its method of assault, the Government should not complain about the obvious difficulties which will be encountered. The built-in inadequacies of attempting to prove incipient foreclosure by a new entity strongly points to the lack of desirability of section 7 application as construed by the Supreme Court. The American economy can ill afford this inventive threat to future growth and experimentation.

V. CONCLUSION

In essence, *Penn-Olin* is but another example of the current dominance of reactionary antitrust enforcement policies. The philosophy of the Department of Justice and the Supreme Court as expressed in the major antitrust cases beginning with *Brown Shoe*¹⁶⁷ results in maintaining arbitrary market structures for the allocation of resources by unduly inhibiting the scope of freedom of contract. The approach centers on such assumptions as (1) the degree of competition is directly proportionate to the number of competitors, (2) short-run effects on competition alone are important, (3) injury to individual competitors equals injury to competition, (4) a firm's size measures its economic power to lessen competition, (5) market share measures a firm's market power, and (6) the degree of concentration in an industry determines competitiveness.¹⁶⁸ These assumptions are but finely honed embellishments of Judge Learned Hand's famous exposition of one view of the social purpose of the antitrust laws: "[I]t is possible, because of its indirect social or moral effect, to prefer a system of small producers, each dependent for his success upon his own skill and character, to one in which the great mass of those engaged must accept direction of a few."¹⁶⁹ Assuming merit to this sophistry if we lived in a stagnant, never changing world, today's technological revolution certainly has taught us that clinging to old business methods will lead to the ultimate disintegration of the non-innovator.¹⁷⁰

¹⁶⁷ *Brown Shoe v. United States*, 370 U.S. 294 (1962).

¹⁶⁸ For an excellent discussion puncturing some common economic assumptions prevalent in today's antitrust enforcement policy, see, Dean & Gustus, *supra* note 119.

¹⁶⁹ *United States v. Aluminum Co. of America*, 148 F.2d 416, 427 (2d Cir. 1945).

¹⁷⁰ "Hand's rhetoric has commended itself to most commentators on the topic, but it seems clear upon reflection that it is a position which is questionable as a description of congressional intent, dubious as social policy, and impossible of antitrust doctrine." Bork & Bowman, *The Crisis in Antitrust*, 65 COLUM. L. REV. 363, 369 (1965). This article is the first in a sequence of five which fully explore the conflicting views currently being advocated on antitrust policy. The others are: Blake & Jones, *In Defense of Antitrust*, 65 COLUM. L. REV. 377 (1965); Bork, *Contrasts in*

The struggle in antitrust law today is essentially a conflict between the social value of encouraging economic progress via business experimentation and the existence of an anti-efficiency backlash through fear of bigness. Courts and enforcement agencies have blurred any meaningful distinction between truly destructive per se type anticompetitive practices—the necessary and proper concern of antitrust policy—and competitive advantages and opportunities gained through superior skill, foresight, and willingness to innovate whether by combination or otherwise.

We are clearly in another era of attacking market structures as such, analogous to the anti-bigness campaigns of the early 1900's. But today's industrial framework and our underlying economy are totally different from this bygone era. A large contemporary corporation is characterized more and more by a wide dispersal of responsibility and decision-making authority within management. There is typically a strong *intra*-corporate as well as *inter*-corporate competition between sales territories, districts, and divisions for increased sales, lower costs, and greater profit margins on the same and dissimilar products. Middle and lower management personnel are responsible for their subordinates and ultimately report to the chief executive officer, *but* are not *directed* like drones by a corporate monarch. Thousands of corporate executives on varying levels within large modern companies have more opportunities to initiate and make decisions than the small shopkeepers, farmers, and tradesmen had at the turn of the century. Increase in the size of business enterprises has *not* concentrated business power into the hands of a few, stifled initiative, or encouraged inefficiency.¹⁷¹ Staffing joint ventures with separate management should remove initially any stigma of the venture being a mere directed instrumentality of the parents.

Closely related to this emergence of professional management is the highly significant rise in consumer purchasing power with discretionary income. Management must constantly anticipate marketing trends, seek to provide better quality products or services, and initiate or be ready to combat the "better mousetrap." Demands for efficiency are endless, but efficiency alone is no saviour in this era of continuous and rapid scientific breakthroughs.

Particularly in the area of joint ventures, effective antitrust policy should forego tying archaic economic concepts to indefinite and unpredictable legal standards and acknowledge that tomorrow's technology will neutralize or overwhelm today's competitive gains.¹⁷² It also is essen-

Antitrust Theory: I, 65 COLUM. L. REV. 401 (1965); Bowman, *Contrasts in Antitrust Theory: II*, 65 COLUM. L. REV. 417 (1965); Blake & Jones, *Toward a Three Dimensional Antitrust Policy*, 65 COLUM. L. REV. 422 (1965). See also Bock, *The Relativity of Economic Evidence in Merger Cases—Emerging Decisions Force the Issue*, 63 MICH. L. REV. 1355 (1965).

¹⁷¹ Handler, *Some Unresolved Problems of Antitrust*, 62 COLUM. L. REV. 930, 951-55 (1962). See Justice Brandeis' dissenting opinion in *Louis K. Liggett Co. v. Lee*, 288 U.S. 517, 541 (1933).

¹⁷² "We have three choices: We can substitute planning for the competitive market; we can keep the market, while distorting its action by government intervention on the false premise that the vigor of competition is determined by the number and size of competitors; or we can recognize that we are moving, year by year, into a more truly competitive and more innovative society in which we will not need and cannot afford the restrictive side of antitrust." Ways, *Antitrust in An Era of Radical Change*, FORTUNE MAGAZINE, March 1966, at 225.

tial in shaping antitrust policy for joint ventures to recognize that they may have the immediate effect of promoting competition even where very large companies are involved. The previously stated economic advantages of venture formation should be accepted as promoting the creation of new technologies and industries in a manner superior to no amalgamation in many cases. Ventures such as Penn-Olin, which are not based on technological progress, also should be encouraged when overall increases in actual competition result. Where a new product, new service, or new production or merchandising method is introduced, a positive, rather than restrictive, approach to joint ventures will result inevitably in overall substantial benefits for consumers and the entire economy.

Southwestern Law Journal

VOLUME 23

May 1969

NUMBER 2

BOARD OF EDITORS

LAWRENCE D. STUART, JR.

Editor-in-Chief

RUFUS S. SCOTT

Managing Editor

DAVID R. SNODGRASS

Leading Articles Editor

STANLEY R. HULLER

Casenotes Editor

BEVERLY A. NEBLETT

Casenotes Editor

FREDERICK W. MARSH, JR.

Comments Editor

MICHAEL M. GIBSON

Research Editor

HUGH T. BLEVINS

Texas Survey Editor

THOMAS W. WEEKS

Business Manager

Associate Editors

ROBERT M. BANDY

JERRY J. FORD

WAYNE L. FRIESNER

GEORGE M. MARIS

JAMES R. CRAIG

Faculty Advisor

JANET P. BALCH

Editorial Assistant

ADVISORY BOARD

Hon. Irving Goldberg
United States Court of Appeals
Dallas, Texas

Hon. James Noel
United States District Court
Houston, Texas

Paul G. Kauper
School of Law
University of Michigan

Joseph T. Sneed
School of Law
Stanford University

Walter Magee, President
Southwestern Law Journal
Alumni Association

Percy Williams
Attorney-at-Law
Houston, Texas

Member, National Conference of Law Reviews