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## Mere Common Ownership and the Antitrust Laws

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# MERE COMMON OWNERSHIP AND THE ANTITRUST LAWS

THOMAS A. LAMBERT

INTRODUCTION .....	2914
I. THE PURPORTED ANTICOMPETITIVE HARMS OF COMMON OWNERSHIP .....	2918
II. SECTION 7 OF THE CLAYTON ACT .....	2924
<i>A. The Areeda-Hovenkamp View</i> .....	2925
<i>B. Professor Elhaug's View</i> .....	2931
1. Purchasing the Stock Solely for Investment .....	2934
2. Not Using the Stock to Bring About, or in Attempting to Bring About, the Substantial Lessening of Competition .....	2940
<i>C. The Correct Interpretation of the Solely-for-Investment Exemption and Its Implications for     Mere Common Ownership</i> .....	2943
III. SECTION 1 OF THE SHERMAN ACT.....	2948
<i>A. The Shareholder Contract Theory</i> .....	2948
<i>B. The Analogy to Historic Trusts and Holding Companies</i> .....	2952
IV. WHY ANTITRUST CONDEMNATION OF MERE COMMON OWNERSHIP WOULD LIKELY REDUCE SOCIAL WELFARE.....	2957
CONCLUSION.....	2962

# MERE COMMON OWNERSHIP AND THE ANTITRUST LAWS

THOMAS A. LAMBERT\*

**Abstract:** “Common ownership,” also called “horizontal shareholding,” refers to a stock investor’s ownership of minority stakes in multiple competing firms. Recent empirical studies have purported to show that institutional investors’ common ownership reduces competition among commonly owned competitors. “Mere common ownership” is horizontal shareholding that is not accompanied by any sort of illicit agreement, such as a hub-and-spoke conspiracy, or the holding of a control-conferring stake. This Article considers the legality of mere common ownership under the U.S. antitrust laws. Prominent antitrust scholars and the leading treatise have concluded that mere common ownership that has the incidental effect of lessening market competition may violate both Section 7 of the Clayton Act and Section 1 of the Sherman Act. This Article, however, demonstrates otherwise. Competition-lessening instances of mere common ownership do not violate Section 7 of the Clayton Act because they fall within its “solely-for-investment” provision, which the scholars calling for condemnation have misinterpreted. Mere common ownership does not run afoul of Section 1 of the Sherman Act because it lacks the sort of agreement (contract, combination, or conspiracy) required for liability under that provision. From a social welfare standpoint, these legal outcomes are desirable. Condemning mere common ownership under the antitrust laws would likely entail significant costs, and the benefits such condemnation would secure are speculative. Accordingly, this Article argues courts and enforcers should not stretch the antitrust laws to condemn mere common ownership.

## INTRODUCTION

In contemporary antitrust parlance, “common ownership” (also called “horizontal shareholding”) refers to a stock investor’s ownership of minority stakes in competing firms. Common ownership is similar to, but distinct from, “cross ownership,” which occurs when one firm owns stock of its competitor or when an investor holding a majority interest in one firm also owns stock of a competing firm.<sup>1</sup> Any mutual fund or exchange-traded fund that holds minority shares

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<sup>1</sup> See Edward B. Rock & Daniel L. Rubinfeld, *Antitrust for Institutional Investors*, 82 ANTITRUST L.J. 221, 232 (2018) (distinguishing “cross ownership” and “common ownership”).

of competing companies is engaged in common ownership.<sup>2</sup> As investment in such funds has proliferated, particularly with the soaring popularity of low-cost index funds, common ownership has become quite significant.<sup>3</sup> Today, the largest providers of mutual and index funds may each own sizable percentages of every major competitor in a market.<sup>4</sup>

A number of antitrust scholars have expressed concerns about this development. Harvard Law School Professor Einer Elhauge, for example, wrote in the *Harvard Law Review* that “[a]n economic blockbuster has recently been exposed”—namely, “[a] small group of institutions has acquired large shareholdings in horizontal competitors throughout our economy, causing them to compete less vigorously with each other.”<sup>5</sup> Eric A. Posner, Fiona M. Scott Morton, and E. Glen Weyl (Posner et al.) echoed Professor Elhauge’s worries that common ownership has anticompetitive effects, writing in the *Antitrust Law Journal* that “the concentration of markets through large institutional investors is the ma-

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<sup>2</sup> A mutual fund is an entity that aggregates money from many individuals and invests it in a professionally managed portfolio of assets, typically stocks of other companies. See U.S. Sec. & Exch. Comm’n, *Mutual Funds*, INVESTOR.GOV, <https://www.investor.gov/introduction-investing/basics/investment-products/mutual-funds-and-exchange-traded-funds-etfs> [<https://perma.cc/KXX9-9RVP>]. Mutual funds provide investors with instant diversification, which reduces their investment risk. *Id.* Like a mutual fund, an exchange-traded fund (ETF) is a diversified investment pool wherein retail investors may purchase shares. See U.S. Sec. & Exch. Comm’n, *Exchange-Traded Funds (ETFs)*, INVESTOR.GOV, <https://www.investor.gov/introduction-investing/basics/investment-products/exchange-traded-funds-etfs> [<https://perma.cc/PGW6-82U8>]. But whereas shares in mutual funds are priced once a day based on the net asset value of the fund (i.e., assets minus liabilities, divided by the number of shares outstanding), shares in ETFs are traded on an exchange at market prices that may differ from the net asset value. *Id.*

<sup>3</sup> An index fund is a mutual fund or ETF that is invested in the companies included in a stock index, which is a pre-determined list of companies designed to represent some sector of the stock market or perhaps the economy as a whole (e.g., the S&P 500 Index). See U.S. Sec. & Exch. Comm’n, *Index Funds*, INVESTOR.GOV, <https://www.investor.gov/introduction-investing/basics/investment-products/index-funds> [<https://perma.cc/ET7C-YRNF>]. The managers of an index fund, unlike those of an actively managed mutual fund or ETF, do not exercise discretion in choosing the companies to invest in. *Id.* Accordingly, index funds generally charge lower management fees than do actively managed funds. *Id.* The combination of instant diversification with very low management fees has drastically boosted the popularity of index funds. See Dawn Lim, *Index Funds Are the New Kings of Wall Street*, WALL STREET J. (Sept. 18, 2019), <https://www.wsj.com/articles/index-funds-are-the-new-kings-of-wall-street-11568799004> [<https://perma.cc/7JMN-D372>] (observing that funds tracking broad U.S. stock indexes held \$4.27 trillion in assets as of August 31, 2019, for the first time surpassing actively managed funds, which then held assets of \$4.25 trillion).

<sup>4</sup> The largest asset managers include Vanguard, BlackRock, State Street Global Advisers, and Fidelity Investments which, for example, may own between 2% and 10% of all competitors in a market. *Mutual Fund Directory | 2020: Top 100 Mutual Fund Companies Ranked by AUM*, MUTUALFUNDDIRECTORY.ORG, <https://mutualfunddirectory.org> [<https://perma.cc/A3D4-PQ87>] (ranking mutual funds by their assets under management) (last updated Aug. 11, 2020).

<sup>5</sup> Einer Elhauge, *Horizontal Shareholding*, 129 HARV. L. REV. 1267, 1267 (2016) [hereinafter Elhauge, *Horizontal Shareholding*] (expressing concern about the anticompetitive effects of horizontal shareholding).

for new antitrust challenge of our time.”<sup>6</sup> Other leading antitrust commentators have concurred that institutional investors’ common ownership poses a competitive threat and may violate the antitrust laws.<sup>7</sup>

Antitrust enforcement agencies have responded to these scholars’ concerns. At a March 2016 hearing before a Senate subcommittee, William J. Baer, then-Assistant Attorney General for the Antitrust Division of the U.S. Department of Justice (DOJ), announced that enforcers were investigating potential antitrust issues stemming from investors’ common ownership of the stock of multiple firms competing in concentrated industries.<sup>8</sup> In March 2018, Margrethe Vestager, European Commissioner of Competition, announced that a similar investigation was under way in the European Union.<sup>9</sup> And in December 2018, the U.S. Federal Trade Commission (FTC) devoted four panels to common ownership as part of its Hearings on Competition and Consumer Protection in the twenty-first century.<sup>10</sup>

These actions raise questions about when exactly common ownership violates the antitrust laws. To be sure, common ownership can be a component of a scheme that injures competition and runs afoul of antitrust prohibitions. Examples of common ownership that violate the antitrust laws include: (1) when an

<sup>6</sup> Eric A. Posner et al., *A Proposal to Limit the Anticompetitive Power of Institutional Investors*, 81 ANTITRUST L.J. 669, 669–70 (2017) [hereinafter Posner et al., *Proposal*]; see also Eric Posner et al., *A Monopoly Donald Trump Can Pop*, N.Y. TIMES (Dec. 7, 2016), <https://www.nytimes.com/2016/12/07/opinion/a-monopoly-donald-trump-can-pop.html> [<https://perma.cc/YEB6-C2QL>] (“The great, but mostly unknown, antitrust story of our time is the astonishing rise of the institutional investor . . . and the challenge that it poses to market competition.”).

<sup>7</sup> See, e.g., Jonathan B. Baker, *Overlapping Financial Investor Ownership, Market Power, and Antitrust Enforcement: My Qualified Agreement with Professor Elhauge*, 129 HARV. L. REV. F. 212, 213 (2016), [https://harvardlawreview.org/wp-content/uploads/2016/03/vol129\\_Baker-2.pdf](https://harvardlawreview.org/wp-content/uploads/2016/03/vol129_Baker-2.pdf) [<https://perma.cc/27N3-S3CU>]; Fiona Scott Morton & Herbert Hovenkamp, *Horizontal Shareholding and Antitrust Policy*, 127 YALE L.J. 2026, 2027 (2018).

<sup>8</sup> Barry A. Nigro, Jr., *Cross-Ownership by Institutional Investors*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Mar. 31, 2016), <https://corpgov.law.harvard.edu/2016/03/31/cross-ownership-by-institutional-investors/#1> [<https://perma.cc/P8P5-87XB>]. Major institutional investors appear to be concerned about regulatory interventions to police common ownership. The world’s largest asset manager—BlackRock, Inc.—recently disclosed in a Securities and Exchange Commission (SEC) filing that its “business operations, reputation or financial condition” could be “adversely affected” by proposed policies to address competition concerns arising from common ownership. BlackRock, Inc., Annual Report (Form 10-K), at 26 (Feb. 28, 2018).

<sup>9</sup> See Margrethe Vestager, Comm’r for Competition, European Comm’n, Speech at Studienvereinigung Kartellrecht International EU Competition Law Forum: A Market That Works for Consumers (Mar. 12, 2018), [https://wayback.archive-it.org/12090/20191129214816/https://ec.europa.eu/commission/commissioners/2014-2019/vestager/announcements/market-works-consumers\\_en](https://wayback.archive-it.org/12090/20191129214816/https://ec.europa.eu/commission/commissioners/2014-2019/vestager/announcements/market-works-consumers_en) [<https://perma.cc/92Q9-QLFH>].

<sup>10</sup> See *FTC Hearing #8: Common Ownership*, FED. TRADE COMM’N (Dec. 6, 2018), <https://www.ftc.gov/news-events/events-calendar/ftc-hearing-8-competition-consumer-protection-21st-century> [<https://perma.cc/JCM3-3XKQ>].

investor facilitates a hub-and-spoke conspiracy<sup>11</sup> by helping multiple competing firms to collude; (2) when a group of investors that all own stakes in multiple competitors agree to pressure those firms to limit competition among themselves; and (3) when a single investor with sufficient managerial control in all the firms in a market causes each firm to limit competition with its rivals.<sup>12</sup> In all of these situations, common ownership *plus something else* that would reduce competition, such as an illicit trade-restraining agreement or ownership stakes sufficient to confer control, would cause antitrust liability to attach.<sup>13</sup>

But what about common ownership simpliciter—that is, horizontal shareholding without an agreement among investors or portfolio firms and lacking an ownership stake sufficient to confer managerial control on a shareholder owning stakes in multiple firms within the market? A number of prominent scholars have asserted that the federal antitrust laws condemn “mere” common ownership that has the incidental effect of reducing competition.<sup>14</sup> They say the practice may violate both the prohibition in Section 7 of the Clayton Act on stock acquisitions that substantially lessen competition in a market<sup>15</sup> and the ban in Section 1 of the

<sup>11</sup> A hub-and-spoke conspiracy, also known as a wheel conspiracy, occurs when “a single member or group . . . separately agrees with two or more other members or groups” to engage in unlawful activity. *Wheel Conspiracy*, BLACK’S LAW DICTIONARY (11th ed. 2019).

<sup>12</sup> Rock & Rubinfeld, *supra* note 1, at 222 (observing that a per se illegal “‘hub and spoke’ conspiracy” would result from portfolio managers “acting as a ‘cartel ringmaster,’ who organized a cartel among the competing [portfolio companies] in order to restrict output and increase prices”); see Douglas H. Ginsburg & Keith Klovers, *Common Sense About Common Ownership*, 2 CONCURRENCES REV. 1, 3 (2018), <https://www.concurrences.com/en/review/issues/no-2-2018/articles/common-sense-about-common-ownership-86847-en> [<https://perma.cc/C9PM-Z6V5>] (describing the modern conception of hub-and-spoke conspiracies). See generally *United States v. Apple, Inc.*, 791 F.3d 290, 314 (2d Cir. 2015) (describing modern hub-and-spoke conspiracies).

<sup>13</sup> The first and second scenarios—a hub-and-spoke conspiracy and an agreement among common owners to pursue a lessening of competition among their portfolio firms—would violate Section 1 of the Sherman Act’s prohibition of contracts, combinations, and conspiracies that unreasonably restrain trade. See 15 U.S.C. § 1 (2018). The third scenario, the ownership of control-conferring interests in competing firms, would violate Section 7 of the Clayton Act if such ownership threatened a “substantial lessening of competition.” See *id.* § 18.

<sup>14</sup> See PHILLIP E. AREEDA & HERBERT HOVENKAMP, *ANTITRUST LAW: AN ANALYSIS OF ANTI-TRUST PRINCIPLES AND THEIR APPLICATION* ¶ 1204b (4th ed. Cum. Supp. 2020); Elhauge, *Horizontal Shareholding*, *supra* note 5, at 1302–04; Einer Elhauge, *How Horizontal Shareholding Harms Our Economy—And Why Antitrust Law Can Fix It*, 10 HARV. BUS. L. REV. 207, 255–56, 269 (2020) [hereinafter Elhauge, *Horizontal Shareholding Harm*]; Posner et al., *Proposal*, *supra* note 6, at 677–78; Scott Morton & Hovenkamp, *supra* note 7, at 2033.

<sup>15</sup> See, e.g., AREEDA & HOVENKAMP, *supra* note 14, ¶ 1203c (“[S]o-called horizontal shareholding is reachable under [Section] 7 where the threat to competition is present. This phenomenon occurs when a relatively small number of investors, typically institutional, acquire large overlapping interests in two or more firms.” (footnote omitted)); Elhauge, *Horizontal Shareholding*, *supra* note 5, at 1302–04 (contending that mere common ownership may violate 15 U.S.C. § 18); Scott Morton & Hovenkamp, *supra* note 7, at 2033–35 (same).

Sherman Act on contracts, combinations, and conspiracies that unreasonably restrain trade.<sup>16</sup>

This Article demonstrates that mere common ownership by institutional investors, even if it incidentally contributes to a softening of competition, does not violate the U.S. antitrust laws. Mere common ownership does not give rise to liability under Section 7 of the Clayton Act because it falls within the provision's "solely-for-investment" exemption, which both Professor Elhaug's scholarship and the leading antitrust treatise have misinterpreted.<sup>17</sup> Mere common ownership is not illegal under Section 1 of the Sherman Act because it entails no trade-restraining contract, combination, or conspiracy.<sup>18</sup> As a policy matter, antitrust law's failure to condemn mere common ownership is a good thing, as the marginal cost of such condemnation would likely exceed the marginal benefit produced.<sup>19</sup>

In developing these points, the Article proceeds as follows: Part I sets the stage by describing the theory as to how mere common ownership may soften competition and briefly summarizes the key empirical studies purporting to support that theory.<sup>20</sup> Part II addresses Section 7 of the Clayton Act and shows that mere common ownership is exempt from that provision's ban on stock acquisitions that may substantially lessen competition.<sup>21</sup> Part III considers Section 1 of the Sherman Act and explains why mere common ownership does not run afoul of that provision's prohibition of trade-restraining contracts, combinations, or conspiracies.<sup>22</sup> Shifting from law to policy, Part IV concludes by explaining why social welfare would likely be reduced if antitrust law did condemn mere common ownership.<sup>23</sup>

## I. THE PURPORTED ANTICOMPETITIVE HARMS OF COMMON OWNERSHIP

The scholars sounding alarm bells over common ownership have theorized that it softens competition by altering the incentives of corporate managers.<sup>24</sup>

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<sup>16</sup> See, e.g., Elhaug, *Horizontal Shareholding Harm*, *supra* note 14, at 269–70 (contending that mere common ownership may violate 15 U.S.C. § 1); Scott Morton & Hovenkamp, *supra* note 7, at 2035–36 (same).

<sup>17</sup> See discussion *infra* Part II.

<sup>18</sup> See discussion *infra* Part III.

<sup>19</sup> See discussion *infra* Part IV.

<sup>20</sup> See discussion *infra* Part I.

<sup>21</sup> See discussion *infra* Part II.

<sup>22</sup> See discussion *infra* Part III.

<sup>23</sup> See discussion *infra* Part IV.

<sup>24</sup> See generally Elhaug, *Horizontal Shareholding*, *supra* note 5, at 1268–70 (arguing that the incentive to reduce prices as a means of increasing profits is diminished by common ownership); Posner et al., *Proposal*, *supra* note 6, at 685–86.

Most of the time, those managers, responding to their shareholders' desires, seek to maximize the profits of their individual firms—*i.e.*, “own-firm” profits. That typically involves growing market share, which entails price and quality competition from which consumers benefit. Even though a firm's profits would normally be greater with collusion than with vigorous competition, the desire to maximize own-firm profits usually generates aggressive price and quality competition. When collusion or tacit coordination emerges and drives up prices, firm managers know that they could earn even greater profits by slightly underpricing their rivals so as to win business, and when one firm cheats in this fashion, others tend to follow suit, causing price coordination to unravel and competition to reemerge.<sup>25</sup> The desire to maximize own-firm profits, then, fosters the sort of competition that maximizes consumer surplus.

Unlike most shareholders, investors holding stock in all the firms in a market—*i.e.*, “intra-industry diversified” investors—prefer that each firm's managers maximize industry profits, rather than own-firm profits. This influences these shareholders' preferences with regard to how vigorously the firms they are invested in compete. When one firm gains market share, it usurps the sales from another firm in which the intra-industry diversified investor also holds a stake. And it typically does so by reducing price or spending more to enhance quality, so its profit margin on the usurped sale is lower. Intra-industry diversified investors would thus prefer that firms limit their price and quality competition to generate the highest *industry*, rather than own-firm, profits.<sup>26</sup>

But why would firm managers defer to intra-industry diversified investors over the shareholders who own the bulk of the stock and who would prefer own-firm profit maximization? The theory is that the largest intra-industry diversified investors—the major institutional investors—are better positioned to influence management. Relative to individual shareholders, these investors possess more extensive monitoring resources and greater expertise on matters of business strategy and firm policy. Additionally, they have greater incentive to monitor the degree that managers are promoting their interests because they hold larger

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<sup>25</sup> As Professor Einer Elhauge explains:

In competitive markets where ownership is separate, economic models prove that firms have incentives to undercut each others' prices because the profits they gain from the additional sales exceed the price reduction caused by their own conduct. Because each firm sets prices based on the same calculus, they keep undercutting each other until they drive down prices toward marginal cost, which is the most efficient level.

Elhauge, *Horizontal Shareholding*, *supra* note 5, at 1269.

<sup>26</sup> *See id.* at 1279 (“For such [intra-industry diversified] institutional investors, managers who increase individual corporate performance by competing with rivals and taking away market share decrease institutional investor profits across the industry by decreasing industry profits. Institutional investors are more likely to prefer managers who maximize industry profits by avoiding competition.”).



stakes.<sup>27</sup> Their votes are also more likely to attract media attention, which gives managers an even greater incentive to secure their favor. Accordingly, corporate managers often honor the preferences of institutional investors over those of individual, uncoordinated stockholders, even when the latter group collectively owns a greater proportion of company stock.<sup>28</sup> Managers may therefore seek to maximize industry profits, which leads them to pull their firms' competitive punches.

There are strong reasons to question whether intra-industry diversified institutional investors will systematically prefer maximization of industry rather than own-firm profits.<sup>29</sup> Similarly, the assertion that corporate managers will defer to institutional investors over the shareholders holding the bulk of their companies' stock is open to doubt.<sup>30</sup> The primary driver of concerns about common ownership, however, has not been theory. Instead, it has been empirical studies purporting to demonstrate that common ownership reduces competition.

In the most prominent of those studies, co-authors José Azar, Martin C. Schmalz, and Isabel Tecu (Azar et al.) attempted to test whether institutional investors' common ownership of the stock of competing domestic airlines increased airfares.<sup>31</sup> To measure common ownership incentives and assess the degree that they changed over time, Azar et al. utilized a metric known as "MHHI

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<sup>27</sup> Eric A. Posner, Fiona M. Scott Morton, and E. Glen Weyl (Posner et al.) emphasize these differences between individual and institutional investors:

The separation of ownership and control that makes possible very large companies leads to managers who are not supervised by a knowledgeable monitor, but only by very small individual shareholders who do not have the time, information, or power to oversee management. Institutional investors by contrast, could potentially improve on this Berle-Means model of the corporation—featuring widely dispersed ownership by shareholders with tiny stakes—by supplying informed and incentivized oversight.

Posner et al., *Proposal*, *supra* note 6, at 674.

<sup>28</sup> According to Posner et al., this conclusion: "[F]ollows from a very simple logic: someone must determine the firm's goals. That controller is likely to be one of the largest shareholders. If there are no large concentrated shareholders, then the firm will likely be run in the interests of its institutional investors even if these do not individually own very large stakes." *Id.* at 684–85.

<sup>29</sup> This premise disregards the fact that intra-industry diversified institutional investors are also *inter-industry* diversified. Their investments in related industries (either vertically related or complementary) will be adversely affected by supracompetitive pricing in the industry that they are intra-industry diversified in, so it is not clear that they would prefer industry profit maximization. See Thomas A. Lambert & Michael E. Sykuta, *The Case for Doing Nothing About Institutional Investors' Common Ownership of Small Stakes in Competing Firms*, 13 VA. L. & BUS. REV. 213, 233–35 (2019).

<sup>30</sup> This premise ignores the fact that firm managers' personal incentives tend to align with those of the bulk of their shareholders in favor of own-firm profit maximization. This is so because (1) most corporate managers' company's stock compensates them in part, and (2) most desire to usurp business from their rivals to burnish their personal reputations for business success. See *id.* at 235–37.

<sup>31</sup> José Azar et al., *Anticompetitive Effects of Common Ownership*, 73 J. FIN. 1513, 1522 (2018) [hereinafter Azar et al., *Anticompetitive Effects*]; see also Lambert & Sykuta, *supra* note 29, at 223 (reviewing empirical evidence that common ownership causes anticompetitive effects).

delta” (MHHIΔ).<sup>32</sup> MHHIΔ is a component of the “modified Herfindahl-Hirschman Index” (MHHI), which is an adjusted version of the well-known Herfindahl-Hirschman Index (HHI) that the antitrust enforcement agencies use in evaluating prospective mergers.<sup>33</sup> The MHHI seeks to account for both the concentration of the relevant market (HHI) and the degree to which common ownership reduces market participants’ incentives to compete. MHHIΔ is the component of MHHI that accounts for reduced competition incentives occasioned by common ownership.<sup>34</sup> Thus, MHHI is equal to the sum of HHI and MHHIΔ.

The objective of MHHIΔ, which is calculated using a complicated formula,<sup>35</sup> is to assess the likelihood that managers of firms within an industry, assuming that they seek to maximize their shareholders’ portfolio returns (weighted by those shareholders’ control), would cause their firms to cut back on price competition in an effort to maximize industry rather than own-firm profits.<sup>36</sup> The primary factors determining the magnitude of MHHIΔ are:

- the amount of voting control intra-industry diversified investors have over the managers of their portfolio firms (MHHIΔ grows as intra-industry diversified investors have greater voting control);
- the magnitude of the stakes intra-industry diversified investors hold in the firms within the industry, and the degree that each investor’s holdings across competing firms are of equal size (the larger the financial stakes held by intra-industry diversified shareholders and the more equal those stakes across the competing firms, the higher the MHHIΔ);
- the degree that the stock (and thus voting control) of firms within the industry is held by *non*-intra-industry diversified shareholders (when there is

<sup>32</sup> Azar et al., *Anticompetitive Effects*, *supra* note 31, at 1522.

<sup>33</sup> See U.S. DEP’T OF JUSTICE & FED. TRADE COMM’N, HORIZONTAL MERGER GUIDELINES 1, 18–19 (2010), <https://www.justice.gov/sites/default/files/atr/legacy/2010/08/19/hmg-2010.pdf> [<https://perma.cc/L2ZJ-HQLT>] (describing how the Herfindahl-Hirschman Index (HHI) is calculated). HHI ranges from near zero to 10,000 and is calculated by adding the squares of the market shares of the firms competing in a market. *Id.* It assesses the degree to which a market is concentrated, and thus susceptible to collusion or oligopolistic coordination. *Id.*

<sup>34</sup> Azar et al., *Anticompetitive Effects*, *supra* note 31, at 1519, 1522.

<sup>35</sup> The precise formula for “MHHI delta” (MHHIΔ) is:

$$\text{MHHI}\Delta = 10,000 \cdot \sum_j \sum_{k \neq j} s_j s_k \left( \frac{\sum_i \beta_{ij} \beta_{ik}}{\sum_i \beta_{ij}^2} \right),$$

where  $\beta_{ij}$  is the fraction of shares in firm  $j$  controlled by investor  $i$ ; the shares are both cash flow and control shares (so control rights are assumed to be proportionate to the investor’s share of firm profits); and  $s_j$  is the market share of firm  $j$ . Azar et al., *Anticompetitive Effects*, *supra* note 31, at 1522; Lambert & Sykuta, *supra* note 29, at 271–78 (providing a non-technical explanation of the formula and detailed instructions for calculating the metric for a particular market).

<sup>36</sup> See Posner et al., *Proposal*, *supra* note 6, at 683–84 (explaining the logic of MHHIΔ). See generally Lambert & Sykuta, *supra* note 29, at 224–25 (describing how MHHIΔ is calculated, its variables, and its significance in antitrust).

- greater control by investors who are not intra-industry diversified and who thus prefer own-firm profit maximization, MHHIA is reduced); and
- the market shares of the firms that share common ownership (when their market shares are larger, the market effect of firm managers' decisions to pull their competitive punches will be more significant, so MHHIA will be higher).<sup>37</sup>

In their airline study, Azar et al. first figured the MHHIA for each domestic airline route—each assumed to be a separate market—from 2001 to 2014. They then examined each route and market to determine how changes in the MHHIA over time correlated with changes in airfares on that route.<sup>38</sup> After running a number of regressions to control for route-specific factors that might influence both fares and the MHHIA,<sup>39</sup> they concluded that common ownership of air carriers increased airfares from 3% to 7%.<sup>40</sup>

A second widely cited common ownership study attempted to assess how common ownership has affected service fees and interest rates in local markets for bank deposits.<sup>41</sup> In that study, co-authors José Azar, Sahil Raina, and Martin C. Schmalz considered how the account fees charged by commercial banks, the minimum account sizes required to avoid such fees (“fee thresholds”), and the interest rates the banks paid on deposits correlated with “generalized HHI” (GHHI), a measure that resembles MHHI.<sup>42</sup> The authors found that for interest-bearing checking accounts, a one standard deviation increase in GHHI correlated with an increase in fees of about 11% and an increase in fee thresholds of around 17%.<sup>43</sup> For money market accounts, a similar increase in GHHI correlated with a

<sup>37</sup> See Lambert & Sykuta, *supra* note 29, at 224–25; Posner et al., *Proposal*, *supra* note 6, at 683–84.

<sup>38</sup> Azar et al., *Anticompetitive Effects*, *supra* note 31, at 1526–28.

<sup>39</sup> *Id.* at 1528–29.

<sup>40</sup> *Id.* at 1559. See generally Lambert & Sykuta, *supra* note 29, at 224–25 (summarizing the José Azar, Martin C. Schmalz, and Isabel Tecu (Azar et al.) study’s empirical approach towards anticompetitive effects in the airline industry). An instrumental variable analysis by the authors found even greater adverse effects. It suggested that common ownership increased airfares between 10% and 12%. Azar et al., *Anticompetitive Effects*, *supra* note 31, at 1559.

<sup>41</sup> José Azar et al., *Ultimate Ownership and Bank Competition 1* (May 4, 2019) (unpublished manuscript), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2710252](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2710252) [<https://perma.cc/MBG4-M5RC>] [hereinafter Azar et al., *Ultimate Ownership*]; see also Lambert & Sykuta, *supra* note 29, at 226–27 (summarizing the empirical model used in Azar et al.’s study on common ownership in banking).

<sup>42</sup> Azar et al., *Ultimate Ownership*, *supra* note 41, at 22–24. The formula for the MHHI, which works when there is either common ownership of competing firms by third-parties or cross-ownership of some firms by others, must be refined if either (1) there is a mixture of common- and cross-ownership, or (2) the cross-ownership involves both cross-owned firms holding stakes in each other (e.g., firm A owns a stake in firm B, and firm B owns a stake in A). See Elhauge, *Horizontal Shareholding*, *supra* note 5, at 1277 n.48. The GHHI incorporates this necessary refinement.

<sup>43</sup> Azar et al., *Ultimate Ownership*, *supra* note 41, at 26–27.

3% increase in fees and a nearly 17% increase in fee thresholds.<sup>44</sup> The authors also found that increases in GHHI correlated with a reduction in the interest rates paid to depositors.<sup>45</sup>

Scholars have criticized the airline and banking studies for endogeneity, given that MHHI and GHHI turn in part on firms' market shares and on the number of firms participating in a market, both of which are affected by demand forces that independently influence market price.<sup>46</sup> Replications designed to avoid such endogeneity and to correct other asserted methodological errors have not found anticompetitive effects from common ownership.<sup>47</sup> Professor Elhauge counters that these methodological criticisms are unfounded,<sup>48</sup> and that the studies finding no anticompetitive effect are flawed.<sup>49</sup> He also points to other, more recent studies that purportedly demonstrate anticompetitive effects from common ownership in the pharmaceutical and seed industries.<sup>50</sup>

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<sup>44</sup> *Id.*

<sup>45</sup> *Id.* at 23; see also Lambert & Sykuta, *supra* note 29, at 226–27 (summarizing the results of Azar et al.'s banking study).

<sup>46</sup> See Lambert & Sykuta, *supra* note 29, at 243–44; Daniel P. O'Brien & Keith Waehrer, *The Competitive Effects of Common Ownership: We Know Less Than We Think*, 81 ANTITRUST L.J. 729, 732 (2017) (“[T]he key explanatory variable in this research—the modified HHI (MHHI)—depends on market shares, which depend on the same underlying factors that drive prices. In econometric terms, market shares and the MHHI are endogenous.”). In addition to these endogeneity criticisms, the studies are deficient because they purport to correlate market outcomes with institutional investors' incentives, but they never accurately assess what those incentives are. Lambert & Sykuta, *supra* note 29, at 238–42. The studies assume that an intra-industry diversified institutional investor must prefer maximization of industry rather than own-firm profits, but that is not at all clear. Institutional investors earn different fees on different funds, and the funds that generate the highest fees tend not to be fully intra-industry diversified. *Id.* at 239–42. If institutional investors prefer to maximize the performance of their highest-margin funds, they may well prefer some market outcome other than industry profit maximization. Because the common ownership studies have not drilled down to the fund level to determine what market outcomes provide the greatest profits to institutional investors, they have not properly assessed institutional investors' preferences, and thus cannot have correlated those preferences with market outcomes, as they claim to have done.

<sup>47</sup> See Patrick Dennis et al., *Common Ownership Does Not Have Anticompetitive Effects in the Airline Industry* 33 (Fed. Reserve Bank of Atlanta, Working Paper No. 15, 2019), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3063465](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3063465) [<https://perma.cc/XR78-48F3>]; Pauline Kennedy et al., *The Competitive Effects of Common Ownership: Economic Foundations and Empirical Evidence* 22–23 (July 26, 2017) (unpublished manuscript), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3008331](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3008331) [<https://perma.cc/WVV9-TH8E>].

<sup>48</sup> Elhauge, *Horizontal Shareholding Harm*, *supra* note 14, at 223–25.

<sup>49</sup> *Id.* at 225–35.

<sup>50</sup> *Id.* at 239–44 (first citing Joseph Gerakos & Jin Xie, *Institutional Horizontal Shareholdings and Generic Entry in the Pharmaceutical Industry* (Mar. 18, 2019) (Tuck Sch. of Bus., Working Paper No. 3285161, 2019), <https://ssrn.com/abstract=3285161> [<https://perma.cc/LY98-2RN4>]; then citing Melissa Newham et al., *Common Ownership and Market Entry: Evidence from Pharmaceutical Industry* (DIW Berlin, Discussion Paper No. 1738, 2019), <https://ssrn.com/abstract=3194394> [<https://perma.cc/9CC9-DQHF>]; and then citing Mohammad Torshizi & Jennifer Clapp, *Price Effects of Common Ownership in the Seed Sector* 33–35 (Apr. 22, 2019) (unpublished manuscript), <https://ssrn.com/abstract=3338485> [<https://perma.cc/ND6B-NLQG>]). Professor Elhauge also cites a cross-market study that found “that

I will not attempt to resolve this debate because the central matter this Article addresses is not the empirical question of whether mere common ownership in fact reduces competition. Instead, the relevant question here is a legal one: whether mere common ownership passes muster under the antitrust laws, even if it incidentally lessens competition. Based on the theory and evidence described above, scholars have argued that mere common ownership may violate both Section 7 of the Clayton Act and Section 1 of the Sherman Act. Parts II and III consider those two provisions in turn, concluding that mere common ownership offends neither.<sup>51</sup>

## II. SECTION 7 OF THE CLAYTON ACT

Section 7 of the Clayton Act, which primarily addresses anticompetitive business mergers, may also restrict partial stock acquisitions.<sup>52</sup> The provision states that “[n]o person engaged in commerce . . . shall acquire . . . the whole *or any part* of the stock . . . of another person engaged also in commerce . . . where in any line of commerce . . . the effect of such acquisition may be substantially to lessen competition.”<sup>53</sup> Although this text expressly addresses only anticompetitive acquisitions of stock, an investor could not avoid liability by showing that none of its discrete purchases of a company’s stock would, standing alone, lessen competition.<sup>54</sup> Allowing acquirers to avoid Section 7’s prohibition by buying up stock in a series of transactions, none of which would independently lessen competition, would create an obvious loophole that could render the provision ineffective. The U.S. Supreme Court has thus concluded that Section 7 forbids not merely acquiring, but also *holding* stock when doing so threatens a “substantial lessening of competition” in a market.<sup>55</sup> In light of that understanding, Professors Elhauge,<sup>56</sup> Scott Morton and Hovenkamp,<sup>57</sup> Posner et al.,<sup>58</sup> as well as the

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higher levels of horizontal shareholding in consumer goods markets resulted in a statistically significant increase in prices.” Elhauge, *Horizontal Shareholding Harm*, *supra* note 14, at 241 (citing Had-iyeh Aslan, *Common Ownership, Creative Destruction, and Inequality: Evidence from U.S. Consumers 8–10* (Sept. 12, 2019) (unpublished manuscript) (on file with author)).

<sup>51</sup> See discussion *infra* Part II (arguing that Section 7 of the Clayton Act does not reach common ownership); discussion *infra* Part III (concluding that common ownership does not violate Section 1 of the Sherman Act).

<sup>52</sup> 15 U.S.C. § 18 (2018) (prohibiting stock acquisition when the effect is “substantially to lessen competition, or to tend to create a monopoly”).

<sup>53</sup> *Id.* (emphasis added).

<sup>54</sup> See *infra* notes 55–59 and accompanying text.

<sup>55</sup> See 15 U.S.C. § 18; *United States v. ITT Cont’l Baking Co.*, 420 U.S. 223, 241 (1975) (observing that “‘acquisition’ can mean, and in the context of [Section] 7 of the Clayton Act does mean, both the purchase of rights in another company and the retention of those rights”).

<sup>56</sup> Elhauge, *Horizontal Shareholding*, *supra* note 5, at 1302–04.

<sup>57</sup> Scott Morton & Hovenkamp, *supra* note 7, at 2035 (“The practices involved in horizontal shareholding generally concern partial stock acquisitions. The same kind of economic theory and

Areeda-Hovenkamp treatise have all concluded that Section 7 forbids mere common ownership that has the likely effect of reducing competition in a market.<sup>59</sup>

A potential difficulty for this view is the first sentence of Section 7's third paragraph, which states that "[t]his section shall not apply to persons purchasing stock solely for investment and not using the same by voting or otherwise to bring about, or in attempting to bring about, the substantial lessening of competition."<sup>60</sup> By its terms, this solely-for-investment provision would seem to exempt investors engaged in mere common ownership—including institutional investors—from Section 7's prohibitions. The scholars contending that Section 7 reaches mere common ownership, however, have advanced two interpretations that would prevent the solely-for-investment provision from insulating institutional investors whose horizontal shareholding threatens a "substantial lessening of competition."

For reasons set forth below, each of those interpretations is flawed.<sup>61</sup> Correctly interpreted, the first sentence of Section 7's third paragraph exempts mere common ownership from Section 7 liability.

#### A. The Areeda-Hovenkamp View

The influential Areeda-Hovenkamp treatise<sup>62</sup> takes the position that Section 7's solely-for-investment language is not a true exemption from potential liability.<sup>63</sup> To be a true exemption, there would have to be some stock acquisition or continued stock holding that would violate Section 7 *except for the fact* that the investor acquired the stock or held it "solely for investment." According to the treatise, such an acquisition or continued holding is an impossibility.

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evidence (conventionally used in merger analysis) justifies using Section 7 against horizontal shareholding.").

<sup>58</sup> Posner et al., *Proposal*, *supra* note 6, at 691 (observing that "[t]he most natural solution" to the competitive problems posed by common ownership "is to simply enforce Section 7 of the Clayton Act").

<sup>59</sup> AREEDA & HOVENKAMP, *supra* note 14, ¶ 1203c ("[H]orizontal shareholding is reachable under [Section] 7 where the threat to competition is present. This phenomenon occurs when a relatively small number of investors, typically institutional, acquire large overlapping share interests in two or more firms." (footnote omitted)).

<sup>60</sup> 15 U.S.C. § 18.

<sup>61</sup> See discussion *infra* Part II.A.

<sup>62</sup> Antitrust lawyers and judges so extensively rely on the Areeda-Hovenkamp treatise that Justice Stephen Breyer once wrote that "most practitioners would prefer to have two paragraphs of Areeda's treatise on their side than three Courts of Appeals or four Supreme Court Justices." Stephen Breyer, *In Memoriam: Phillip E. Areeda*, 109 HARV. L. REV. 889, 890 (1996).

<sup>63</sup> AREEDA & HOVENKAMP, *supra* note 14, ¶ 1204a ("[I]s [the solely-for-investment provision] truly an 'exception' that immunizes an acquisition that the courts would otherwise deem to violate [Section] 7? We reach a negative answer . . .").

Key to the treatise's position is its view that an investor should be presumed to intend the likely consequences of its actions. Under this view, no stock acquisition that would be likely at the time of purchase to lessen competition could be solely for investment, as the investor would be purchasing with an "intent" to secure an anticompetitive outcome.<sup>64</sup> Moreover, the continued holding of legally purchased shares would cease to be "solely for investment" at the very moment such continued holding became likely to lessen competition (so that the stockholder was "intending" something beyond investment). The upshot of this reasoning is that there can be no stock acquisition or continued stock holding that would (1) otherwise violate Section 7's substantive prohibitions, but (2) be insulated from liability because it was solely for investment. As such, the treatise concludes, Section 7's solely-for-investment language creates no actual exemption or defense.

The treatise offers three reasons for taking this view.<sup>65</sup> First, it says, "permitting anticompetitive investment is directly contrary to the central purpose of the Clayton Act."<sup>66</sup> Second, there are a few brief remarks in the legislative history suggesting Congress included the solely-for-investment provision to ease concerns that the Clayton Act would condemn the ordinary investment practices of colleges and banks, and the committee reports in both the House and Senate stated that "the exceptions [made in Section 7] are those which are not deemed monopolistic and do not tend to restrain trade."<sup>67</sup> Third, as a policy matter, preserving market competition is more important than "protecting particular portfolio diversification," because "[r]arely is a given investment opportunity uniquely advantageous."<sup>68</sup> The Areeda-Hovenkamp treatise's argument is flawed for a few reasons.

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<sup>64</sup> The treatise states:

The "true exception" issue would squarely arise only in an acquisition that is deemed both (a) to be solely for investment and (b) to have a probable anticompetitive effect. But there could be no such case if the acquirer were presumed to intend the probable consequences of its act. In that event, a court's finding that the acquisition would probably tend substantially to lessen competition would necessarily mean that the acquirer so intended, objectively speaking. Consequently, its acquisition could not be solely for investment.

*Id.* ¶ 1204b (footnote omitted).

<sup>65</sup> See *infra* notes 66–68 and accompanying text.

<sup>66</sup> AREEDA & HOVENKAMP, *supra* note 14, ¶ 1204b.

<sup>67</sup> *Id.* ¶ 1204b n.8 (first quoting H.R. REP. NO. 63-627, at 17 (1914); then quoting S. REP. NO. 63-698, at 13 (1913)).

<sup>68</sup> *Id.* ¶ 1204b.

The obvious problem with the treatise's interpretation is that it renders the solely-for-investment provision a nullity.<sup>69</sup> Section 7's substantive prohibitions, set forth in the provision's first two paragraphs, regulate three things: (1) asset acquisitions, (2) full mergers where one entity acquires all the stock of a corporation, and (3) partial stock acquisitions.<sup>70</sup> The solely-for-investment language in Section 7's third paragraph clearly could not apply to asset acquisitions (as it refers to "persons purchasing *such stock* solely for investment") or to full mergers (because taking all stock entails a transfer of managerial control, so the acquired stock would not be held "solely for investment"). To have any effect whatsoever, the provision would have to influence the legality of partial stock acquisitions. But under the Areeda-Hovenkamp interpretation, it would not do so because any stock acquisition or holding that is illegal under Section 7's substantive prohibitions (*i.e.*, it is likely to reduce competition substantially) could not be "solely for investment" and thus would remain illegal. The legal outcome would be exactly the same if the first sentence of Section 7's third paragraph were excised from the statute.

The treatise maintains that despite the solely-for-investment provision's legal insignificance, it would still "serv[e] the much more limited function of reassuring investors that the Clayton Act was not designed to interfere with general investment."<sup>71</sup> But it would do no such thing. The substantive prohibitions of Section 7 forbid stock acquisitions only when their effect "may be substantially

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<sup>69</sup> The Areeda-Hovenkamp treatise concedes this point. *See id.* (acknowledging that its interpretation conflicts with "the general canon of statutory construction that seeks to give significance to each statutory provision rather than to make any provision superfluous").

<sup>70</sup> The first two paragraphs of Section 7 of the Clayton Act state:

No person engaged in commerce or in any activity affecting commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital and no person subject to the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets of another person engaged also in commerce or in any activity affecting commerce, where in any line of commerce or in any activity affecting commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly.

No person shall acquire, directly or indirectly, the whole or any part of the stock or other share capital and no person subject to the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets of one or more persons engaged in commerce or in any activity affecting commerce, where in any line of commerce or in any activity affecting commerce in any section of the country, the effect of such acquisition, of such stocks or assets, or of the use of such stock by the voting or granting of proxies or otherwise, may be substantially to lessen competition, or to tend to create a monopoly.

15 U.S.C. § 18.

<sup>71</sup> AREEDA & HOVENKAMP, *supra* note 14, ¶ 1204b.



to lessen competition, or to tend to create a monopoly.”<sup>72</sup> Absent such likely effect, general investment is not forbidden.<sup>73</sup> Investors receive no comfort from an additional provision stating that their investment activities will not be illegal unless their effect “may be substantially to lessen competition,” for that is implied in the substantive liability provisions themselves. Under the Areeda-Hovenkamp reading, then, the solely-for-investment provision does nothing; it is pure surplusage.

The three reasons the treatise asserts for reading the solely-for-investment provision out of the statute are unconvincing. First, the fact that anticompetitive investment is contrary to the Clayton Act’s central purpose cannot justify simply ignoring a statutory exemption. Most of what antitrust regulates is “mixed bag” conduct—*i.e.*, business activities that may create both harms and benefits such that some instances of the behavior will impose net harms and others net benefits.<sup>74</sup> For that reason, antitrust law deliberately tolerates some anticompetitive instances of behavior to avoid deterring efficient ones.<sup>75</sup> Antitrust doctrine is also sensitive to administrative costs and thus sometimes restricts liability for anticompetitive conduct to keep those costs in check.<sup>76</sup> Indeed, much of contemporary antitrust doctrine represents a calculated effort to minimize the sum of social welfare losses from permitting anticompetitive instances of behavior, deterring procompetitive instances, and administering the rules.<sup>77</sup> The Areeda-Hovenkamp treatise’s willingness to render the solely-for-investment provision

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<sup>72</sup> 15 U.S.C. § 18.

<sup>73</sup> *Id.*

<sup>74</sup> See Thomas A. Lambert, *The Limits of Antitrust in the 21st Century*, 68 U. KAN. L. REV. 1097, 1100–02 (2020) (offering examples of antitrust-regulated behaviors that are sometimes output-reducing and sometimes output-enhancing).

<sup>75</sup> For example, although it is well-understood that competition may be harmed by so-called “limit” pricing, which occurs when a firm with market power sets its prices above its costs but below the profit-maximizing level, so as to deter entry, see HERBERT HOVENKAMP, *THE ANTITRUST ENTERPRISE: PRINCIPLE AND EXECUTION* 161–62 (2005), simple discounts are not condemned unless they result in below-cost pricing. The law tolerates some potential anticompetitive harm to avoid deterring procompetitive pricing. See *Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 223, 229 (1993) (holding that below-cost pricing is required for predatory pricing liability because “the exclusionary effect of prices above a relevant measure of cost either reflects the lower cost structure of the alleged predator, and so represents competition on the merits, or is beyond the practical ability of a judicial tribunal to control without courting intolerable risks of chilling legitimate price cutting” (emphasis added)).

<sup>76</sup> See, e.g., *Pacific Bell Tel. Co. v. Linkline Commc’ns, Inc.*, 555 U.S. 438, 452 (2009) (“Institutional concerns also counsel against recognition of such claims. We have repeatedly emphasized the importance of clear rules in antitrust law.”); *Town of Concord v. Bos. Edison Co.*, 915 F.2d 17, 25 (1st Cir. 1990) (“[A]ntitrust courts normally avoid direct price administration, relying on rules and remedies . . . that are easier to administer.”).

<sup>77</sup> See generally Thomas A. Lambert, *The Roberts Court and the Limits of Antitrust*, 52 B.C. L. REV. 871 (2011) (discussing the Roberts Court’s decision-theoretic approach to antitrust and its implications).

surplusage because anticompetitive investment is inconsistent with the central purpose that the Clayton Act implicitly embraces the view that any activity that threatens competition must be condemned. Such an absolutist position is inappropriate in the antitrust arena, especially when (1) the behavior at issue offers obvious benefits, and (2) attempts to restrict it would entail large administrative costs. For reasons set forth in Part IV, intra-industry diversification by institutional investors is exactly that sort of behavior.<sup>78</sup>

Second, the legislative history of the solely-for-investment provision does not justify reading it out of the statute, as the Areeda-Hovenkamp interpretation would do. As an initial matter, a statute's enacted text, which here speaks of an actual exemption ("[t]his section shall not apply to"), must trump unenacted legislative history.<sup>79</sup> Beyond that, it is not at all clear that the legislative history of Section 7 supports the view the Areeda-Hovenkamp treatise espouses. For example, in the debates on the Clayton Act, U.S. Senator George W. Norris remarked that "[n]obody wants to prohibit a savings bank or individual or an institution investing their funds in the stock of corporations, whether they are competing or not, if they do not use that method for controlling the corporations."<sup>80</sup> Those remarks suggest that Congress intended the solely-for-investment provision to provide a genuine exemption that would turn not on the incidental competitive effect of acquiring or continuing to hold stock, but on whether the stock was being *used to control* the company at issue. As explained in Section C of this Part, a proper interpretation of the solely-for-investment provision is much closer to that understanding than to the Areeda-Hovenkamp treatise's view that the language has no legal significance.<sup>81</sup>

The treatise's third argument for reading the provision as surplusage is that "the public interest in competitive markets far outweighs the private interest in protecting particular portfolio diversification" because "[r]arely is a given investment opportunity uniquely advantageous."<sup>82</sup> But the relative social value of

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<sup>78</sup> See *infra* notes 242–249 and accompanying text (discussing the high administrative costs of MHHI-based lawsuits); *infra* notes 252–260 and accompanying text (discussing investor benefits from low-cost index funds and other intra-industry diversified mutual funds).

<sup>79</sup> See 15 U.S.C. § 18; e.g., *Graham Cty. Soil & Water Conservation Dist. v. United States ex rel. Wilson*, 559 U.S. 280, 302 (2010) (Scalia, J., concurring) ("The Constitution gives legal effect to the 'Laws' Congress enacts . . . not the objectives its Members aimed to achieve in voting for them." (citing U.S. CONST. art. VI, cl. 2)); *Murphy v. Millennium Radio Grp. LLC*, 650 F.3d 295, 303 (3d Cir. 2011) (explaining that legislative history cannot trump the plain terms of a statute, absent rare circumstances); *MDY Indus., LLC v. Blizzard Entm't, Inc.*, 629 F.3d 928, 951 (9th Cir. 2010) (stating that policy "considerations cannot trump the statute's plain text and structure" in construing Section 1201(a) of the Digital Millennium Copyright Act); *Knurr v. Orbital ATK Inc.*, 276 F. Supp. 3d 527, 540 (E.D. Va. 2017) ("Legislative history, however, cannot trump plain text.").

<sup>80</sup> 51 CONG. REC. 14,466 (1914) (statement of Sen. Norris).

<sup>81</sup> See discussion *infra* Part II.C.

<sup>82</sup> AREEDA & HOVENKAMP, *supra* note 14, ¶ 1204b.

competitive markets versus diversification opportunities for investors is ultimately a legislative judgment. Congress could well have determined that the benefits of affording non-controlling shareholders diversification freedom likely outweigh any incremental competitive gains from limiting that freedom. Had Congress reached that conclusion, it would have included exemption language resembling the first sentence of Section 7's third paragraph. What is more, the sort of investment conduct exempted by this Article's interpretation of the solely-for-investment provision (set forth in Section C of Part II) is "uniquely advantageous."<sup>83</sup> Part IV explains why that is so.<sup>84</sup>

Ultimately, the Areeda-Hovenkamp treatise's interpretation of Section 7's solely-for-investment provision fails because the treatise wrongly equates a likely adverse effect on competition with non-investment intent (*i.e.*, it assumes that if a stock purchase would likely impair competition, it could not have been "solely for investment").<sup>85</sup> That interpretation is inconsistent with a natural read-

<sup>83</sup> See discussion *infra* Part II.C.

<sup>84</sup> See discussion *infra* Part IV.

<sup>85</sup> See 15 U.S.C. § 18. The Areeda-Hovenkamp treatise cites two cases in support of its view that a purchase or holding of stock cannot be "solely for investment" if it is likely to cause anticompetitive effect. See AREEDA & HOVENKAMP, *supra* note 14, ¶ 1204b n.7 (first citing *In re Golden Grain Macaroni Co.*, 78 F.T.C. 63, 72 (1971), *modified*, 472 F.2d 882 (9th Cir. 1972); then citing *Gulf & W. Indus., Inc. v. Great Atl. & Pac. Tea Co.*, 476 F.2d 687, 693 (2d Cir. 1973)). Professors Fiona Scott Morton and Herbert Hovenkamp cite the same two cases in support of their claim that "[t]wo courts of appeal agree that the [solely-for-investment] section was meant as little more than an assurance to purely passive investors rather than as a limitation on the Clayton Act's coverage." Scott Morton & Hovenkamp, *supra* note 7, at 2042. The two cited cases, however, hardly justify reading the solely-for-investment language out of the statute, as the treatise interpretation, endorsed by Professors Scott Morton and Hovenkamp, would do. The relevant discussion in *In re Golden Grain Macaroni Co.* in 1971, which appeared in the Federal Trade Commission's (FTC) administrative decision and was never addressed in the U.S. Court of Appeals for the Ninth Circuit's opinion, concerned an acquisition that would "necessarily" reduce competition. 78 F.T.C. at 73 ("[W]hen an acquisition will necessarily affect the competitive behavior of the two involved firms, it cannot be said that the *sole* purpose of the acquisition was for investment."). To say that one must intend a necessary effect of their actions is not to imply that they intend the effects that are only likely, particularly if they have no reason to know that they are likely. See *infra* notes 180–185 and accompanying text (observing that the common ownership studies find a softening of competition resulting from the industry's overall pattern of stock ownership, which individual investors are typically unaware). In 1973, in *Gulf & Western Industries, Inc. v. Great Atlantic & Pacific Tea Co., Inc.*, the U.S. Court of Appeals for the Second Circuit construed a precedent on the solely-for-investment provision as "say[ing] no more than that the court's attention should be focused less on whether the purchase constitutes an 'investment' than on whether the effect (indeed at this juncture the *reasonably likely* effect) is substantially to lessen competition." 476 F.2d at 693 (citing *Pa. R.R. Co. v. Interstate Commerce Comm'n*, 66 F.2d 37, 40 (3d Cir. 1933) (*per curiam*), *aff'd by an equally divided court*, 291 U.S. 651 (1934)). But that statement was obiter dictum, given the court's conclusion that the record did not reflect investment-only intent. See *id.* at 694 (observing that "the record demonstrates . . . that G&W [the investor] will seek to obtain control of A&P [the portfolio company] and that it has the potential to attain that goal"). Moreover, the *Gulf & Western* court engaged in no analysis of the statutory text and blatantly misconstrued *Pennsylvania Railroad Co. v. Interstate Commerce Commission*, in which the U.S. Court of Appeals for the Third

ing of the text, which speaks of the purchaser's purpose in buying the stock, not its intent about the stock purchase's incidental effect on competition. More importantly, the treatise's interpretation would, for no compelling reason, render the solely-for-investment provision superfluous.

### B. Professor Elhauge's View

Professor Elhauge has offered an interpretation of the solely-for-investment provision that avoids nullifying the provision but would still exclude intra-industry diversified institutional investors from its protection.<sup>86</sup> That interpretation, however, reads the exemption too narrowly. It is inconsistent with (1) the case law construing the solely-for-investment provision,<sup>87</sup> (2) agency regulations defining "solely for the purpose of investment,"<sup>88</sup> (3) the meaning of investment under the federal securities laws,<sup>89</sup> and (4) Section 7's plain text.<sup>90</sup>

As Professor Elhauge correctly observes, Section 7's investment exemption includes two elements. First, the stock must have been purchased "solely for investment."<sup>91</sup> Second, the stock must not be "us[ed] . . . by voting or otherwise to bring about, or in attempting to bring about, the substantial lessening of competition."<sup>92</sup> The first element is met, Professor Elhauge says, only if the investor refrains from voting its shares (or engages in only "mirror voting"<sup>93</sup>), and otherwise exercises no influence over corporate managers.<sup>94</sup> The second element re-

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Circuit interpreted the solely-for-investment provision as creating a genuine exemption, the first element turns on the stock investor's intent in purchasing the stock. See *Gulf & W. Indus., Inc.*, 476 F.2d at 693–94 (citing *Pa. R.R. Co.*, 66 F.2d at 39–40)).

<sup>86</sup> As explained below, Professor Elhauge has proposed two interpretations of the solely-for-investment provision. Both would exclude intra-industry diversified institutional investors from liability protection, but only one would avoid rendering the provision superfluous. See *infra* note 99 and accompanying text. This Section discusses only the interpretation that would not nullify the solely-for-investment provision. The alternative interpretation should be rejected for the same reasons as the Areeda-Hovenkamp treatise's interpretation.

<sup>87</sup> See *infra* notes 102–121 and accompanying text.

<sup>88</sup> See 15 U.S.C. § 18; *infra* notes 122–132 and accompanying text.

<sup>89</sup> See *infra* notes 133–141 and accompanying text.

<sup>90</sup> See *infra* notes 142–153 and accompanying text.

<sup>91</sup> 15 U.S.C. § 18.

<sup>92</sup> *Id.*

<sup>93</sup> Elhauge, *Horizontal Shareholding*, *supra* note 5, at 1306. "Mirror voting" is voting one's shares in the proportions wherein all other shares are voted. Doing so ensures that one's shares are counted to establish a quorum, but do not influence the outcome of the vote. Thomas A. DeCapo & Kenneth E. Burdon, *Proposed Amendments to the Federal Proxy Rules: Considerations for Closed-End Funds*, SKADDEN, ARPS, SLATE, MEAGHER & FLOM LLP (Nov. 20, 2019), <https://www.skadden.com/insights/publications/2019/11/proposed-amendments-to-the-federal-proxy-rules> [https://perma.cc/GL58-PUFX] (defining "mirror vot[ing]" in the context of the SEC's changes to the federal proxy rules in November 2019).

<sup>94</sup> Elhauge, *Horizontal Shareholding*, *supra* note 5, at 1306 ("The solely-for-investment element has been found to be met only when the investor committed either to not vote its stock or (in what

quires that the investor's stock ownership not contribute to an actual "lessen[ing] of competition" or an attempt to do so.<sup>95</sup> The upshot of this interpretation is that, if an investor satisfies the first element by committing to pure passivity (no voting or engagement with management), that commitment changes the showing required to establish liability from *likely* anticompetitive effect to *actual or intended* anticompetitive harm.<sup>96</sup>

Unlike the Areeda-Hovenkamp interpretation, this construal would not render the solely-for-investment provision superfluous, for it would be possible for a stock acquisition to violate the substantive prohibition of Section 7, and yet be immunized by the provision. Suppose an investor buying stock in multiple competitors committed not to vote its shares or to attempt to influence the management of any of the rival firms. After its purchase, other investors also bought shares in multiple firms within the industry, so that the overall pattern of com-

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amounts to the same thing) to vote the shares in the same proportion as other shareholders vote, often with the additional requirements that the investor not nominate directors, have any representative on the board, or exert any other form of influence over management."); Elhauge, *Horizontal Shareholding Harm*, *supra* note 14, at 256 (asserting that "a stock acquisition can be solely for investment only if the investor does not vote or otherwise influence corporate behavior at all").

<sup>95</sup> Elhauge, *Horizontal Shareholding*, *supra* note 5, at 1308 (observing that even if investors purchased stock solely for investment, "proof that their horizontal shareholdings actually lessened competition . . . would negate the passive investor exception and leave the horizontal shareholders subject to challenge under [Section] 7 of the Clayton Act" (footnote omitted)).

<sup>96</sup> *Id.* at 1308 ("Whereas an active investment can be condemned if it *may* substantially lessen competition, a passive investment can be condemned only if it *actually* does so or was intended to do so."). Specifically, this interpretation shifts the standard of liability from "may be substantially to lessen competition" (i.e., likely anticompetitive effects) to "bring[ing] about, or attempt[ing] to bring about, the substantial lessening of competition" (i.e., actual or intended harm). *Id.* at 1302, 1309 (quoting 15 U.S.C. § 18). Professor Elhauge has more recently written that:

[E]ven if a stock acquisition were solely for investment, that does not really create an exception, but rather merely changes the standard of proof from "may" substantially lessen competition to instead require evidence that the stock acquisition was intended to have anticompetitive effects or actually has or likely would have anticompetitive effects.

Elhauge, *Horizontal Shareholding Harm*, *supra* note 14, at 256. That latter statement requires amendment. The U.S. Supreme Court has clarified that the language "may . . . substantially . . . lessen competition" in Section 7's substantive prohibition means that the acquisition is reasonably likely to lessen competition. *See* 15 U.S.C. § 18; *United States v. Penn-Olin Chem. Co.*, 378 U.S. 158, 171 (1964) (observing that requirements for liability under Section 7 "are satisfied when . . . the 'reasonable likelihood' of a substantial lessening of competition in the relevant market is shown"); *United States v. E.I. du Pont de Nemours & Co.*, 353 U.S. 586, 607 (1957) ("We repeat, that the test of a violation of [Section] 7 is whether, at the time of suit, there is a reasonable probability that the acquisition is likely to result in the condemned restraints."); *see also United States v. Sungard Data Sys., Inc.*, 172 F. Supp. 2d 172, 180 (D.D.C. 2001) ("To establish a [s]ection 7 violation, plaintiff must show that a pending acquisition is reasonably likely to cause anticompetitive effects."). Accordingly, if purchasing stock solely for investment "changes the standard of proof," it must alter the standard to require "actual[]" or "intended . . . anticompetitive effects," not merely a likelihood of "anticompetitive effects." Elhauge, *Horizontal Shareholding Harm*, *supra* note 14, at 256.

mon ownership became *likely* to soften competition. At that point, the substance of Section 7 would be violated by the first investor's continued common ownership within the industry (as such holding would contribute to a likely "lessening of competition"), but the investor's common ownership would be exempt from liability until an anticompetitive effect *actually materialized* or the investor *intended* such a reduction in competition. Professor Elhaug's proffered interpretation would thus give the solely-for-investment provision a legal effect so that it would not be mere surplusage.

At the same time, the interpretation would not insulate intra-industry diversified institutional investors from damages liability under Section 7. The exemption's first element would rarely be satisfied by institutional investors, Professor Elhaug explains, because they almost always vote their shares and often engage with the management of their portfolio firms.<sup>97</sup> Even if an institutional investor committed to pure passivity at the time of its purchase, as soon as the pattern of common ownership actually resulted in higher prices or reduced quality—the moment a plaintiff could claim damages—the investor would lose the exemption's protection.<sup>98</sup> Professor Elhaug has therefore provided an interpretation of the solely-for-investment provision that would afford it legal effect, avoiding surplusage, while preventing it from immunizing institutional investors against damages liability under Section 7.<sup>99</sup>

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<sup>97</sup> Elhaug, *Horizontal Shareholding*, *supra* note 5, at 1306 (observing that "institutional investors with a passive investment strategy usually do actively seek to influence corporate management, including by direct communication, having investor executives serve on corporate boards, and voting their shares to favor positions and management that best advance their investor interests"); Elhaug, *Horizontal Shareholding Harm*, *supra* note 14, at 256 ("[A] stock acquisition can be solely for investment only if the investor does not vote or otherwise influence corporate behavior at all, which is rarely the case for leading horizontal shareholders.").

<sup>98</sup> Elhaug, *Horizontal Shareholding*, *supra* note 5, at 1308 ("[E]ven if investors who held horizontal stock were purely passive, proof that their horizontal shareholdings actually lessened competition, such as the Azar, Schmalz, and Tecu study showing that horizontal shareholdings actually raised airline prices, would negate the passive investor exception and leave the horizontal shareholders subject to challenge under [Section] 7 of the Clayton Act." (citing Azar et al., *Anticompetitive Effects*, *supra* note 31, at 1558–59)).

<sup>99</sup> Professor Elhaug has actually proposed two interpretations of the solely-for-investment provision. The other interpretation, however, would render the provision a nullity. He writes:

[F]or investors who are completely passive, proving the substantive standard [of liability under Section 7] requires showing that the investors are "using the [purchase of stock] by voting or otherwise to bring about, or in attempting to bring about, the substantial lessening of competition." I think *the better reading* of this language is that this standard can be met prophylactically if, at the time of the stock acquisitions, it can be shown that the purchases of stock were intended to substantially lessen competition or foreseeably would have that effect because they lessen competitive incentives. In those cases, the investors are using the purchase of stock to bring about, or attempt to bring about, a substantial lessening of competition. But one can imagine a *narrow reading* of

There are, however, problems with Professor Elhaug's interpretation. Although he correctly reads Section 7's "solely for investment" language as providing an actual exemption if two elements are satisfied, he has misread each of those two elements.

### 1. Purchasing the Stock Solely for Investment

First, Professor Elhaug has construed the first element of the exemption—that the investor "purchas[ed] such stock solely for investment"—too narrowly. He contends that "a stock acquisition can be solely for investment only if the investor does not vote or otherwise influence corporate behavior at all."<sup>100</sup> He further maintains that:

The solely-for-investment element has been found to be met only when the investor committed either to not vote its stock or (in what amounts to the same thing) to vote the shares in the same proportion as other shareholders vote, often with the additional requirements that the investor not nominate directors, have any representative on the board, or exert any other form of influence over management.<sup>101</sup>

In actuality, neither the cases applying the solely-for-investment provision nor agency regulations defining the phrase "solely for the purpose of investment" support Professor Elhaug's strict interpretation of the exemption's first element.

No case holds that merely voting one's shares or making any effort, however slight, to influence management is inconsistent with purchasing or holding stock solely for investment. For example, in *United States v. Tracinda Investment Corp.*,<sup>102</sup> which Professor Elhaug cites as support for his narrow construal of the solely-for-investment element,<sup>103</sup> the U.S. District Court for the Central District of California explained that an investor's purchase of nineteen percent of

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the statute that, for completely passive investors, requires waiting until their stock acquisitions actually have those anticompetitive effects before a challenge can be brought.

*Id.* at 1309 (emphasis added) (quoting 15 U.S.C. § 18). Under the interpretation that Professor Elhaug refers to as "the better reading," the likelihood that a stock purchase would lessen competition substantially—the trigger for liability under Section 7's substantive prohibition—would preclude the investment exemption from applying. *See id.* Thus, the solely-for-investment provision would have no legal effect because the legal outcome would be the same if the language were excised from the statute (i.e., with or without the language, stock purchases or holdings that made it likely that competition would be lessened would be forbidden, while those that did not do so, would not be). The discussion in the text has therefore focused on Professor Elhaug's "narrow reading," which would create an actual exemption and thus would not render the solely-for-investment language superfluous. *See id.*

<sup>100</sup> Elhaug, *Horizontal Shareholding Harm*, *supra* note 14, at 256.

<sup>101</sup> Elhaug, *Horizontal Shareholding*, *supra* note 5, at 1306.

<sup>102</sup> *United States v. Tracinda Inv. Corp.*, 477 F. Supp. 1093, 1097–98 (C.D. Cal. 1979).

<sup>103</sup> Elhaug, *Horizontal Shareholding*, *supra* note 5, at 1306 n.191.

a company's stock was "solely for investment," even though the investor, in making its purchase, had procured a contractual commitment from the target company that its management would consult with the investor's sole shareholder on management restructuring and major financial issues.<sup>104</sup> The district court held that this commitment to consult with the investor's principal was not inconsistent with a purchase "solely for investment" because the agreement mandating consultation provided that "[n]othing in this section shall limit the absolute and unfettered discretion of [the target] after such advice and consultation to act on such matters in any manner it deems appropriate."<sup>105</sup> But providing advice and consultation to a firm's management involves *influencing* managers' decisions even if the managers are free to reject the proffered advice.<sup>106</sup> Professor Elhauge's claim that "a stock acquisition can be solely for investment only if the investor does not vote or otherwise influence corporate behavior at all" is thus inconsistent with *Tracinda*.<sup>107</sup>

*Anaconda Co. v. Crane Co.*,<sup>108</sup> which Professor Elhauge also cites, does not support his view that purchasing stock "solely for investment" precludes voting one's shares.<sup>109</sup> In that case, the U.S. District Court for the Southern District of New York held that the buyer's planned purchase of 22.6% of a company's stock was solely for investment where the buyer promised not to buy any more of the company's stock, seek representation on its board, or "vot[e] to bring about or attempt to bring about a substantial lessening of competition."<sup>110</sup> The investor did not promise to refrain from voting entirely or to engage in only mirror voting; rather, it promised not to vote *so as to achieve or attempt a "substantial lessening of competition."*<sup>111</sup> Thus, *Anaconda* in no way implies that merely voting one's shares negates investment-only intent.

A third case Professor Elhauge cites in support of his crabbed view of the solely-for-investment element is *United States v. E.I. du Pont de Nemours &*

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<sup>104</sup> *Tracinda Inv. Corp.*, 477 F. Supp. at 1100–01 (quoting 15 U.S.C. § 18).

<sup>105</sup> *Id.* at 1101 (first alteration in original) (first quoting Plaintiff's Exhibit 262, at p. 5; then quoting 15 U.S.C. § 18).

<sup>106</sup> Notably, both the president of the portfolio company and one of its board members "testified that they w[ould] listen to [the shareholder's] advice and consultation." *Id.* Yet, the U.S. District Court for the Central District of California concluded that "the stock acquisition in question was made solely for investment purposes and was not made with any intent to take over active managerial control of [the portfolio company], or for any purpose other than investment." *Id.*

<sup>107</sup> Elhauge, *Horizontal Shareholding Harm*, *supra* note 14, at 256; see *Tracinda Inv. Corp.*, 477 F. Supp. at 1100–01.

<sup>108</sup> *Anaconda Co. v. Crane Co.*, 411 F. Supp. 1210, 1218–19 (S.D.N.Y. 1975).

<sup>109</sup> 15 U.S.C. § 18; Elhauge, *Horizontal Shareholding*, *supra* note 5, at 1306 n.191.

<sup>110</sup> *Anaconda Co.*, 411 F. Supp. at 1217.

<sup>111</sup> *Id.*



Co.<sup>112</sup> In that case, the Supreme Court held that a large block of a company's stock (twenty-three percent) was not purchased "solely for investment."<sup>113</sup> According to Professor Elhauge, "the passive investment exception did not apply because the investor tried to influence business decisions" of its portfolio company.<sup>114</sup> The Court's conclusion, however, did not rest on the mere fact that the investor, du Pont, attempted to exert influence at the acquired firm, General Motors (GM).

Documents contemporaneous with du Pont's purchase showed that its objective in buying GM stock was not simply to earn *investment* income through GM dividends, but also to enhance du Pont's *own sales* by convincing GM to use du Pont as a supplier.<sup>115</sup> The Court explained:

[B]efore the first block of General Motors stock was acquired, du Pont was seeking markets [for various of its products] . . . in demand by the automobile companies. In that connection, the trial court expressly found that ". . . reports and other documents written at or near the time of the investment show what du Pont's representatives were well aware [of:] that General Motors was a large consumer of products of the kind offered by du Pont," and that John J. Raskob, du Pont's treasurer and the principal promoter of the investment, "for one, thought that du Pont would ultimately get all that business . . . ."<sup>116</sup>

Referencing a du Pont Treasurer's Report that recommended the GM stock purchase, the Court observed that "[t]hat report makes clear that more than just a profitable investment was contemplated. A major consideration was that an expanding General Motors would provide a substantial market needed by the burgeoning du Pont organization."<sup>117</sup> The Court also pointed to du Pont shareholder reports from the time of the purchase. Those reports echoed the point "that the purchase [of GM stock] would result in du Pont's obtaining a new and substantial market" for its own products.<sup>118</sup> The Court concluded that "[t]his background of the acquisition, particularly the plain implications of the contemporaneous documents, destroys any basis for a conclusion that the purchase was

<sup>112</sup> Elhauge, *Horizontal Shareholding*, *supra* note 5, at 1306 n.190 (citing *E.I. du Pont Nemours & Co.*, 353 U.S. at 597–606).

<sup>113</sup> *E.I. du Pont de Nemours & Co.*, 353 U.S. at 602, 607 (quoting 15 U.S.C. § 18).

<sup>114</sup> Elhauge, *Horizontal Shareholding*, *supra* note 5, at 1306 (citing *id.* at 597–606).

<sup>115</sup> *E.I. du Pont de Nemours & Co.*, 353 U.S. at 600–02.

<sup>116</sup> *Id.* at 600 (quoting *United States v. E.I. du Pont de Nemours & Co.*, 126 F. Supp. 235, 243 (N.D. Ill. 1954), *rev'd*, 353 U.S. 586 (1957)).

<sup>117</sup> *Id.* at 601.

<sup>118</sup> *Id.* at 602.

made ‘solely for investment.’”<sup>119</sup> Thus, *du Pont* holds only that stock bought with the intent of using it to enhance the buyer’s profits *in another line of business* could not have been purchased “solely for investment.”<sup>120</sup> The case does not suggest that merely “tr[ying] to influence business decisions” of the firm whose stock was purchased is inconsistent with investment-only intent.<sup>121</sup>

In addition to lacking support in the case law, Professor Elhaug’s narrow construal of the solely-for-investment element is inconsistent with the meaning of the phrase “solely for the purpose of investment,” which is used elsewhere in the antitrust laws.<sup>122</sup> The Hart-Scott-Rodino Antitrust Improvements Act of 1976—designed, as the title indicates, to improve the implementation of the antitrust laws (primarily Section 7 of the Clayton Act)—requires that certain major purchases of business interests be reported to the government prior to their consummation.<sup>123</sup> The Act posits reporting thresholds,<sup>124</sup> and it provides some statutory exemptions from its requirements.<sup>125</sup> It also authorizes the FTC, with the concurrence of DOJ, to define particular terms in the statute<sup>126</sup> as well as to create certain additional regulatory exemptions for transactions “which are not likely to violate the antitrust laws.”<sup>127</sup> Two of the Act’s statutory exemptions apply only if the transaction is “solely for the purpose of investment.”<sup>128</sup> In addition, the FTC has created two regulatory exemptions that similarly turn on whether the purchase at issue was “solely for the purpose of investment.”<sup>129</sup>

<sup>119</sup> *Id.*

<sup>120</sup> *Id.* (quoting 15 U.S.C. § 18).

<sup>121</sup> See Elhaug, *Horizontal Shareholding*, *supra* note 5, at 1306.

<sup>122</sup> See *infra* notes 123–139 and accompanying text.

<sup>123</sup> Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 18a(a) (requiring persons who plan to acquire “voting securities or assets” of another firm, absent an applicable exemption, to file information with the federal antitrust agencies if the value of the acquired assets exceeds \$50 million (in 2004 dollars) and the acquirer and target are sufficiently large).

<sup>124</sup> *Id.* § 18a(a) (setting criteria for when reporting is required).

<sup>125</sup> *Id.* § 18a(c) (creating exemptions from the reporting requirement).

<sup>126</sup> *Id.* § 18a(d)(2)(a) (authorizing the FTC and Department of Justice (DOJ) to “define the terms used in this section”).

<sup>127</sup> *Id.* § 18a(d)(2)(b) (authorizing the FTC and DOJ to “exempt, from the requirements of this section, classes of persons, acquisitions, transfers, or transactions which are not likely to violate the antitrust laws”).

<sup>128</sup> *Id.* § 18a(c)(9) (exempting “acquisitions, solely for the purpose of investment, of voting securities, if, as a result of such acquisition, the securities acquired or held do not exceed 10 per centum of the outstanding voting securities of the issuer”); *id.* § 18a(c)(11) (exempting “acquisitions, solely for the purpose of investment, by any bank, banking association, trust company, investment company, or insurance company, of (A) voting securities pursuant to a plan of reorganization or dissolution; or (B) assets in the ordinary course of its business”).

<sup>129</sup> 16 C.F.R. § 802.9 (2020) (exempting “[a]n acquisition of voting securities . . . if made solely for the purpose of investment and if, as a result of the acquisition, the acquiring person would hold ten percent or less of the outstanding voting securities of the issuer, regardless of the dollar value of voting securities so acquired or held”); *id.* § 802.64(b) (exempting certain purchases of voting securities if “(1) [m]ade directly by an institutional investor; (2) [m]ade in the ordinary course of business; (3)

For purposes of implementing these statutory and regulatory exemptions, the FTC has exercised its statutory authority to define the phrase “solely for the purpose of investment.” It adopted a rule stating that “[v]oting securities are held or acquired ‘solely for the purpose of investment’ if the person holding or acquiring such voting securities has no intention of participating in the formulation, determination, or direction of the basic business decisions of the issuer.”<sup>130</sup> In promulgating that rule, the FTC explained that the purpose of the definition was to limit the statutory and regulatory exemptions discussed above “to situations in which the acquiring person or the holder has no intention of participating in the management of the issuer.”<sup>131</sup> It expressly rejected the view that merely voting one’s shares (or intending to do so) would be inconsistent with purchasing “solely for the purpose of investment.” It explained:

[C]omments were invited on the suggestion that this definition be further limited by requiring that stock purchased for investment purposes not be voted. The comments . . . were unanimously negative, arguing that voting for directors, without more, was not inconsistent with investment purpose. The Commission has decided not to incorporate this limitation into the final definition. Therefore, merely voting the stock will not be considered evidence of an intent inconsistent with investment purpose.<sup>132</sup>

If merely voting one’s stock is not inconsistent, for purposes of the statute intended to improve Section 7, with having purchased the stock “solely for the purpose of investment,” then it hardly makes sense to say that such voting would prevent a stock purchase from being “solely for investment” under Section 7 itself.

The understanding of “solely for investment” that emerges from the case law and from the definition of a nearly identical phrase elsewhere in the antitrust laws—that purchasing “solely for investment” requires the absence of any intent to participate in management but does not preclude voting one’s stock or offering non-binding advice to managers—aligns with the meaning of “investment” in the federal securities laws.<sup>133</sup> Both the Securities Act of 1933 and the Securi-

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[m]ade solely for the purpose of investment; and (4) [a]s a result of the acquisition the acquiring person would hold fifteen percent or less of the outstanding voting securities of the issuer”).

<sup>130</sup> *Id.* § 801.1(i)(1).

<sup>131</sup> Premerger Notification; Reporting and Waiting Period Requirements, 43 Fed. Reg. 33,450, 33,465 (July 30, 1978) (codified at 16 C.F.R. pts. 801–803).

<sup>132</sup> *Id.*

<sup>133</sup> *Cf. Tracinda Inv. Corp.*, 477 F. Supp. at 1101 (quoting 15 U.S.C. § 18) (finding that stock purchase by a corporation whose sole shareholder had a contractual right to confer with the management of a portfolio company was solely for investment because the purchase “was not made with any

ties Exchange Act of 1934 define the term “security” to include any “investment contract.”<sup>134</sup> In 1946, the Supreme Court originally defined “investment contract” in *Securities & Exchange Commission v. W.J. Howey, Co.* to mean “a contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party.”<sup>135</sup> The Court has since suggested that the expected profits need not be *solely* from the efforts of others, observing that “the ‘touchstone’ of the *Howey* test ‘is the presence of an investment in a common venture premised on a reasonable expectation of profits to be derived from the entrepreneurial or managerial efforts of others.’”<sup>136</sup> The ten circuit courts that have addressed the issue have unanimously concluded that *Howey*’s “solely” language is not to be literally construed and that the crux of the matter is whether the party contributing money has meaningful control over the management of the enterprise generating profits.<sup>137</sup>

Additionally, when applying the test to limited liability company (LLC) interests, which sometimes qualify as investment contracts and sometimes do not,<sup>138</sup> courts have concluded that merely voting a minority share does not constitute sufficient management control to prevent the interest from being an investment contract.<sup>139</sup> The implication is that voting a non-controlling interest,

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intent to take over active managerial control of [the portfolio company], or for any purpose other than investment”).

<sup>134</sup> Securities Act of 1933 § 2, 15 U.S.C. § 77b(a)(1); Securities Exchange Act of 1934 § 3, 15 U.S.C. § 78c(a)(10).

<sup>135</sup> *SEC v. W.J. Howey, Co.*, 328 U.S. 293, 298–99 (1946).

<sup>136</sup> *Int’l Bhd. of Teamsters, Chauffeurs, Warehousemen & Helpers of Am. v. Daniel*, 439 U.S. 551, 561 (1979) (quoting *United Hous. Found., Inc. v. Forman*, 421 U.S. 837, 852 (1975)).

<sup>137</sup> *Rivanna Trawlers Unlimited v. Thompson Trawlers, Inc.*, 840 F.2d 236, 240 n.4 (4th Cir. 1988); *SEC v. Prof’l Assocs.*, 731 F.2d 349, 357 (6th Cir. 1984); *Goodwin v. Elkins & Co.*, 730 F.2d 99, 103 (3d Cir. 1984); *Kim v. Cochenour*, 687 F.2d 210, 213 n.7 (7th Cir. 1982); *SEC v. Aqua-Sonic Prods. Corp.*, 687 F.2d 577, 582 (2d Cir. 1982); *Baurer v. Planning Grp., Inc.*, 669 F.2d 770, 779 (D.C. Cir. 1981); *Williamson v. Tucker*, 645 F.2d 404, 418 (5th Cir. 1981); *Aldrich v. McCulloch Props., Inc.*, 627 F.2d 1036, 1040 n.3 (10th Cir. 1980); *Fargo Partners v. Dain Corp.*, 540 F.2d 912, 914–15 (8th Cir. 1976); *SEC v. Glenn W. Turner Enters., Inc.*, 474 F.2d 476, 482 (9th Cir. 1973). The remaining circuits have suggested agreement with their sister circuits. *See SEC v. SG Ltd.*, 265 F.3d 42, 55 (1st Cir. 2001) (observing that “[t]he courts of appeals have been unanimous in declining to give a literal meaning to the word ‘solely’” in the definition of an investment contract, but not reaching the issue because the scheme under consideration involved profits “solely” from the efforts of others); *SEC v. Unique Fin. Concepts, Inc.*, 196 F.3d 1195, 1201 (11th Cir. 1999) (adopting the *Forman* test that omits the strict “solely” requirement (referring to *Forman*, 421 U.S. at 852)).

<sup>138</sup> *See, e.g., Robinson v. Glynn*, 349 F.3d 166, 174–75 (4th Cir. 2003) (declining to adopt categorical rule on whether LLC membership interests are investment contracts, and observing that answer will differ among companies depending on the degree of managerial control possessed by LLC members).

<sup>139</sup> *See, e.g., United States v. Leonard*, 529 F.3d 83, 89–91 (2d Cir. 2008) (holding that LLC membership interests were securities even though members voted); *Venezia Amos, LLC v. Favret*, No. 3:07cv146/MCR, 2008 WL 410163, at \*8 (N.D. Fla. Feb. 12, 2008) (holding that LLC member-

standing alone, is not the sort of management that transforms the purchase and ownership of the interest into something beyond investment. Such understanding coheres with the FTC's rule that voting alone will not prevent shares of stock from being held "solely for the purpose of investment" and is inconsistent with Professor Elhauge's view that mere voting will negate investment-only intent for purposes of the solely-for-investment provision.

## 2. Not Using the Stock to Bring About, or in Attempting to Bring About, the Substantial Lessening of Competition

Professor Elhauge's reading of the exemption's second element—the requirement that the investor not "us[e] the [purchased stock] by voting or otherwise to bring about, or in attempting to bring about, the substantial lessening of competition"—is also flawed.<sup>140</sup> He says that the requirement is not met, and the exemption's protection is therefore lost, if an investor's stock purchase contributes to an actual "lessening of competition."<sup>141</sup> That would mean that, even if an investor purchased stock in competing firms "solely for investment," the investor could not escape liability under Section 7 if the overall pattern of common ownership in the industry came to reduce competition and cause prices to rise. Accordingly, economic evidence akin to the airline study could create liability for intra-industry diversified investors even if they made each of their stock purchases "solely for investment."<sup>142</sup>

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ship interests were securities "[e]ven assuming that [a member] has voting rights and may inspect the company's records"); *Burnett v. Rowzee*, No. SACV07-641 DOC (ANx), 2007 WL 2809769, at \*3–5 (C.D. Cal. Sept. 26, 2007) (holding that LLC membership interests were securities even though members had a right to, and did, oust manager by majority vote); *SEC v. Parkersburg Wireless Ltd. Liab. Co.*, 991 F. Supp. 6, 7–8 (D.D.C. 1997) (holding that LLC membership interests were securities, even though members voted on a potential acquisition of another company).

<sup>140</sup> Elhauge, *Horizontal Shareholding*, *supra* note 5, at 1309 (quoting 15 U.S.C. § 18).

<sup>141</sup> 15 U.S.C. § 18; Elhauge, *Horizontal Shareholding*, *supra* note 5, at 1308 ("Whereas an active investment can be condemned if it *may* substantially lessen competition, a passive investment can be condemned only if it *actually* does so or was intended to do so."); Elhauge, *Horizontal Shareholding Harm*, *supra* note 14, at 256 (asserting that purchasing stock "solely for investment . . . changes the standard of proof from 'may' substantially lessen competition to instead require evidence that the stock acquisition was intended to have anticompetitive effects or actually has or likely would have anticompetitive effects"). As explained above, courts have interpreted the phrase "may be substantially to lessen competition" in Section 7's substantive prohibitions to mean "is likely" to lessen competition substantially, so if purchasing solely for investment changes the standard for liability, it must raise it to require actual or intended "lessening of competition." *See* 15 U.S.C. § 18; *supra* note 96 and accompanying text.

<sup>142</sup> 15 U.S.C. § 18; Elhauge, *Horizontal Shareholding*, *supra* note 5, at 1308 ("[E]ven if investors who held horizontal stock were purely passive, proof that their horizontal shareholdings actually lessened competition, such as the Azar, Schmalz, and Tecu study showing that horizontal shareholdings actually raised airline prices, would negate the passive investor exception and leave the horizontal shareholders subject to challenge under [Section] 7 of the Clayton Act." (citing Azar et al., *Anticompetitive Effects*, *supra* note 31, at 1558–59)).

This interpretation is inconsistent with the plain meaning of the statutory text. The second element of the solely-for-investment provision requires “not using” purchased stock “to bring about, or in attempting to bring about, the substantial lessening of competition.”<sup>143</sup> Professor Elhauge interprets this language to mean not *causing* a “substantial lessening of competition” with the stock purchase (or intending to do so). But “using” something “to bring about, or in attempting to bring about” some end connotes more than a mere causal relationship between the thing and the end at issue.<sup>144</sup> For example, if a driver deliberately drove a car into a pedestrian, we would say the driver “used” the car “to bring about” the pedestrian’s injuries. By contrast, if the driver accidentally dozed off and steered into a pedestrian, we might say that the car “caused” the pedestrian’s injuries, but we would not say the driver “used” the car “to bring about” harm to the pedestrian. The verbal formula “use *x* to bring about *y*” signals more than just a causal relationship between *x* and *y*; it connotes the intentional availment of *x* for the purpose of achieving *y*.

The Supreme Court’s unanimous decision in *Leocal v. Ashcroft* is instructive on this point.<sup>145</sup> The Court addressed whether Florida’s crime of driving under the influence of alcohol (DUI), which included no *mens rea* element, was a “crime of violence” as defined by 18 U.S.C. § 16.<sup>146</sup> That provision, enacted as part of the Comprehensive Crime Control Act of 1984, defined crime of violence to include “an offense that has as an element the use, attempted use, or threatened use of physical force against the person or property of another.”<sup>147</sup> The issue before the Court was “whether state DUI offenses similar to the one in Florida, which either do not have a *mens rea* component or require only a showing of negligence in the operation of a vehicle, qualify as a crime of violence” under § 16.<sup>148</sup> The issue required the Court to decide whether negligently or unintentionally causing injury by driving while intoxicated could still involve “the use . . . of physical force against the person or property of another” and thereby qualify as a crime of violence under the statute.<sup>149</sup>

The petitioner was an immigrant who had been deported for purportedly committing a “crime of violence” by causing serious bodily injury by driving under the influence of alcohol. He contended that the word “use” entails inten-

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<sup>143</sup> 15 U.S.C. § 18.

<sup>144</sup> *Id.*

<sup>145</sup> *Leocal v. Ashcroft*, 543 U.S. 1, 9 (2004).

<sup>146</sup> *Id.* at 6–7 (citing 18 U.S.C. § 16 (2018)).

<sup>147</sup> 18 U.S.C. § 16(a). The statute also includes in its definition “any other offense that is a felony and that, by its nature, involves a substantial risk that physical force against the person or property of another may be used in the course of committing the offense.” *Id.* § 16(b).

<sup>148</sup> *Leocal*, 543 U.S. at 3–4.

<sup>149</sup> *Id.* at 6–7 (citing 18 U.S.C. § 16(a)).

tional action.<sup>150</sup> The Government argued otherwise, pointing to dictionary definitions, legislation, and even some other Supreme Court decisions suggesting that “use” may be inadvertent or negligent.<sup>151</sup> In resolving the interpretive dispute, the Court explained:

Whether or not the word “use” alone supplies a *mens rea* element, the parties’ primary focus on that word is too narrow. Particularly when interpreting a statute that features as elastic a word as “use,” we construe language in its context and in light of the terms surrounding it. The critical aspect of § 16(a) is that a crime of violence is one involving the “use . . . of physical force *against the person or property of another*.” . . . As we said in a similar context[,]. . . “use” requires active employment. While one may, in theory, actively employ *something* in an accidental manner, it is much less natural to say that a person actively employs physical force against another person by accident. Thus, a person would “use . . . physical force against” another when pushing him; however, we would not ordinarily say a person “use[s] . . . physical force against” another by stumbling and falling into him. When interpreting a statute, we must give words their “ordinary or natural” meaning. The key phrase in § 16(a)—the “use . . . of physical force against the person or property of another”—most naturally suggests a higher degree of intent than negligent or merely accidental conduct. Petitioner’s DUI offense therefore is not a crime of violence under § 16(a).<sup>152</sup>

The interpretive lesson here is that the word “use” (or a variant thereof) may imply intent by the actor and, to decide whether that is the case, one should read the word “in its context and in light of the terms surrounding it” and then ask whether its most “‘ordinary or natural’ meaning” entails intent.<sup>153</sup> When a statute refers to “using” something “to bring about” a particular outcome, the most “‘ordinary or natural’ meaning” is that the actor actively employs the thing with the intent of securing the outcome produced.<sup>154</sup> By contrast, the most “ordinary or natural” way to express Professor Elhauge’s interpretation of the second element would be to eschew the phrase “not using . . . to bring about” in favor of

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<sup>150</sup> *Id.* (“Petitioner contends that his conviction did not require the ‘use’ of force against another person because the most common employment of the word ‘use’ connotes the *intentional* availment of force, which is not required under the Florida DUI statute.”).

<sup>151</sup> *Id.* at 7.

<sup>152</sup> *Id.* (citations omitted) (first quoting *Bailey v. United States*, 516 U.S. 137, 145 (1995); then quoting *Smith v. United States*, 508 U.S. 223, 228 (1993); and then quoting 18 U.S.C. § 16(a)).

<sup>153</sup> *Id.* (quoting *Smith*, 508 U.S. at 228).

<sup>154</sup> *Id.* (quoting *Smith*, 508 U.S. at 228).

language such as “not causing or attempting to cause” “the substantial lessening of competition.” Thus, the better reading of the second element of the solely-for-investment provision as actually enacted is that it forbids actively employing one’s stock with the intent of lessening competition substantially. The mere fact that one’s stockholding contributes to a “lessening of competition,” if the stockholder does not intend that outcome and actively employ the stock to achieve it, will not prevent the exemption’s second element from being satisfied.

*C. The Correct Interpretation of the Solely-for-Investment Exemption and Its Implications for Mere Common Ownership*

The Areeda-Hovenkamp treatise misconstrues the solely-for-investment provision because it wrongly equates a likely adverse effect on competition with a non-investment purpose by the investor, and that error renders the provision a nullity.<sup>155</sup> Professor Elhauge correctly recognizes that the provision creates a genuine exemption that will apply if two elements are satisfied, but he misconstrues each of those elements.<sup>156</sup> Properly construed, the solely-for-investment provision means the following:

Section 7’s prohibition on stock acquisitions that may substantially lessen competition in a market shall not apply if: (1) the investor purchased its stock “solely for investment,” meaning that (a) its only purpose in buying the stock was to earn dividends or to profit from the stock’s appreciation in value, not to enhance profits from its own business operations,<sup>157</sup> and (b) the investor did not intend to, or actually, exercise managerial control over the company at issue, meaning that it could engage in activities typical of mere investors (for example, it could vote a non-controlling percentage of shares or offer non-binding advice to managers) but could not possess actual decision-making authority at the company (for example, it could not hold a management or director position at the company or vote a controlling share of the company’s stock);<sup>158</sup> and (2) the investor did not use the purchased stock to bring about, or in attempting to bring about, the “substantial lessening of competition,” meaning that it did not (a) exercise its rights as a shareholder, (b) with the specific intent of lessening competition.<sup>159</sup>

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<sup>155</sup> See discussion *supra* Part II.A.

<sup>156</sup> See discussion *supra* Part II.B.

<sup>157</sup> See *supra* notes 112–121 and accompanying text (discussing the *du Pont* Court’s conclusion that stock purchase was not “solely for investment” because the purchaser sought to use its influence from investment to boost its own sales).

<sup>158</sup> See discussion *supra* Part II.B.1.

<sup>159</sup> See discussion *supra* Part II.B.2. If an investor exercised its stockholder rights with the specific intent of lessening competition and succeeded in achieving that objective, it would have used the stock “to bring about . . . the substantial lessening of competition.” 15 U.S.C. § 18. If it did not suc-



Under this correct interpretation of the solely-for-investment provision, mere common ownership by an institutional investor will not violate Section 7, even if it incidentally contributes to a lessening of market competition. The first element of the exemption will be satisfied as long as (1) the institutional investor holds a non-controlling share of each company's stock (so that it is engaged in common, not cross-, ownership);<sup>160</sup> (2) no agent or affiliate of the institutional investor takes a management or directorial position at any of the competing portfolio companies (as doing so would mean that the investor is engaged in more than mere common ownership); and (3) the stock was not purchased to earn non-investment income (as in *du Pont*).<sup>161</sup> The second element will be satisfied as long as the institutional investor does not exercise its shareholder rights (for example, voting or offering non-binding advice) *with the intent* of inducing any firm to compete less vigorously. Such intentional efforts to bring about a "lessening of competition" go beyond mere common ownership.

Critics may challenge this analysis on two grounds.<sup>162</sup> First, they may contend that the first element of the solely-for-investment exemption is not satisfied because a large institutional investor exercises de facto managerial control over its portfolio firms. The theory of anticompetitive harm from common ownership holds that corporate managers pursue the interests of their largest shareholders, even when those shareholders own only a small percentage of the company's stock, because the other shareholders are disorganized, poorly informed, and consequently less likely to exert voting pressure on managers.<sup>163</sup> In the words of Posner et al., "someone must determine the firms' goals. That controller is likely to be one of the largest shareholders. If there are no large concentrated shareholders, then the firm will likely be run in the interests of its institutional investors even if these do not individually own very large stakes."<sup>164</sup> If an institutional investor necessarily exerts control over managerial decision making, then it could not have purchased its stock "solely for investment."<sup>165</sup>

It is unlikely, though, that an institutional investor engaged in mere common ownership actually holds the sway that Posner et al. suppose it does. If the

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ceed in lessening competition, it still would have used the stock "in attempting to bring about[] the substantial lessening of competition." *Id.*

<sup>160</sup> See *supra* note 1 and accompanying text (distinguishing "cross[-]ownership" and "common ownership").

<sup>161</sup> See *supra* notes 112–121 and accompanying text (explaining that *du Pont*'s purchase of GM stock was not "solely for investment" because its motivation for purchase was to induce GM to purchase *du Pont* components).

<sup>162</sup> See *infra* notes 163–176 and accompanying text.

<sup>163</sup> See *supra* notes 27–28 and accompanying text.

<sup>164</sup> Posner et al., *Proposal*, *supra* note 6, at 684–85.

<sup>165</sup> *Golden Grain Macaroni Co.*, 78 F.T.C. at 73 (quoting 15 U.S.C. § 18) ("[W]hen an acquisition will necessarily affect the competitive behavior of the two involved firms, it cannot be said that the sole purpose of the acquisition was for investment.").

institutional investor has not assumed a management position and owns only the percentage typically held by a large mutual fund provider (less than 10% of voting securities), it can seldom determine the outcome of a shareholder vote. A recent analysis of proxy voting at the companies included in the Russell 3000 Index, a broad-based index comprised of the 3,000 largest U.S. public companies by market capitalization, revealed that votes are rarely so close that an institutional investor could alter the outcome by changing its vote.<sup>166</sup> In director elections, fewer than 1% of outcomes would have changed if a 10% shareholder had switched its vote, and only 5% would have come out differently if three 10% shareholders had changed their votes in the same direction.<sup>167</sup> For votes on executive compensation packages (“say-on-pay”), only 3% of outcomes would have changed if a 10% investor switched its vote, and only 13% would have changed if three shareholders of that size had done so uniformly.<sup>168</sup> For votes related to mergers and acquisitions,<sup>169</sup> a switch by a 10% shareholder would have altered the outcome in only 1% of votes, and a concerted switch by three 10% shareholders would have changed only 5% of vote outcomes.<sup>170</sup> For shareholder proposals, which comprised a mere 2% of ballot items at Russell 3000 firms, institutional investors could have more sway.<sup>171</sup> In 23% of shareholder proposal votes, a changed vote by a single 10% investor would have altered the outcome, and a uniform vote change by three 10% shareholders could have altered the vote outcome in 67% of shareholder proposal votes.<sup>172</sup> The data also revealed, however, that the major institutional investors often vote differently on shareholder proposals.<sup>173</sup> For example, State Street supported 33% of shareholder proposals, while Vanguard voted affirmatively only 15% of the time.<sup>174</sup> It does not seem, then, that institutional investors vote as a block on shareholder proposals. These data suggest that an institutional investor engaged in mere com-

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<sup>166</sup> See BLACKROCK, PROXY VOTING OUTCOMES: BY THE NUMBERS 1 (2019), <https://www.blackrock.com/corporate/literature/whitepaper/policy-spotlight-proxy-voting-outcomes-by-the-numbers-april-2019.pdf> [<https://perma.cc/F7E6-WXC8>].

<sup>167</sup> *Id.*

<sup>168</sup> *Id.* at 2 (observing that “during the 2017–2018 proxy season, 79% of say-on-pay proposals were approved with greater than 90% support by all shareholders and 87% were won by margins greater than 30%. Only 3% of say-on-pay proposals were won or lost by a margin of 10% or less”).

<sup>169</sup> The category of mergers and acquisitions-related (“M&A-related”) votes includes both votes to approve a merger or acquisition and votes to authorize the financing for such a transaction. *Id.*

<sup>170</sup> *Id.* (observing that “93% of M&A-related votes during the 2017-2018 proxy season received 90% or more support and only one transaction (1%) was passed within a margin of 10% or less [. . . and,] [l]ikewise, less than 5% of transactions passed within a 30% margin”).

<sup>171</sup> *Id.* at 3.

<sup>172</sup> *Id.*

<sup>173</sup> *Id.*

<sup>174</sup> *Id.*

mon ownership, whose only actual “management” consists of voting its shares, will not have de facto managerial control over its portfolio firms.

Second, critics may contend that the second element of the solely-for-investment exemption is not satisfied by an institutional investor engaged in mere common ownership. They would argue that an investor holding shares in competing firms likely lessens competition, as the airline and banking studies purportedly reveal, and the investor should be taken to “intend” the likely effects of its actions.<sup>175</sup> Thus, an institutional investor that receives dividends from competing portfolio firms or votes its shares is exercising its shareholder rights with the intent of lessening competition and is thus “using . . . [its stock] to bring about, or in attempting to bring about, the substantial lessening of competition” under Section 7 of the Clayton Act.<sup>176</sup>

Even if one assumes that mere common ownership does have the likely effect of lessening competition substantially, a point not conceded here,<sup>177</sup> there are two problems with this reasoning.<sup>178</sup> First, it would be improper in this context to presume that the probable effect must have been intended by those causing it. Presuming that an actor intended the likely effect of the actor’s conduct may be appropriate when the actor knows, or at least has reason to know, that the effect is indeed likely to follow from those actions.<sup>179</sup> But when an actor is not privy to the information needed to predict the effect of the actor’s conduct, the mere fact that the effect was likely to result from that behavior does not suggest that actor intended, when acting, to bring about that effect. That is the situation with common ownership.

The theory that common ownership lessens competition, and the empirical studies purporting to support it, assume that corporate managers attempt to maximize the control-weighted portfolio returns of their investors.<sup>180</sup> In other words, a manager considers *all* the stockholdings of the company’s investors, deter-

<sup>175</sup> This resembles the position taken by the Areeda-Hovenkamp treatise. *See supra* notes 62–68 and accompanying text. This position is somewhat different because the treatise reasons that likely anticompetitive effect prevents a stock purchase from being “solely for investment” (element one of the exemption), whereas the claim here is that a likely “lessening of competition” negates the second element of the exemption (not exercising one’s stockholder rights with the intent of “lessening competition”) because a stockholder constructively intends the likely effect of its actions. *See* 15 U.S.C. § 18; *supra* notes 62–68 and accompanying text.

<sup>176</sup> 15 U.S.C. § 18.

<sup>177</sup> *See* Lambert & Sykuta, *supra* note 29, at 233–48 (criticizing theory and evidence of anticompetitive harm from common ownership).

<sup>178</sup> *See infra* notes 179–185 and accompanying text.

<sup>179</sup> Even this is doubtful. *See, e.g.,* Cominelli v. Rector & Visitors of Univ. of Va., 589 F. Supp. 2d 706, 716–17 (W.D. Va. 2008) (“Mere knowledge of a possible result of certain actions, without more, cannot constitute an intentional interference.”).

<sup>180</sup> *See* O’Brien & Waehrer, *supra* note 46, at 739, 742–43 (explaining logic of MHHIA, the metric used to assess incentives to reduce competition).

mines what competitive strategies would maximize the overall portfolio returns of the different investors, weights those potential strategies according to the control each investor exerts over the manager's company (*i.e.*, a large shareholder's preferred strategy gets more weight than that preferred by a small shareholder), and causes the company to pursue whatever strategy dominates.<sup>181</sup> Whether an investor's common ownership is likely to cause a company to pull its competitive punches therefore depends on how that company's stock is distributed among its investors *and* the composition of those investors' portfolios. Because an investor—even a sophisticated institutional investor—would not know who else owns company stock, how much they own, and which other companies they are invested in, it would have no reason to know whether its purchase or continued holding of stock would be likely to cause a “substantial lessening of competition.” Even if the investor's purchase or continued holding were likely to lessen competition substantially, it would be inappropriate to presume that the investor—ignorant of the facts that would demonstrate such likelihood—intended that probable effect. And absent such intent, the investor could not be “*using* the [stock] . . . to bring about, or in attempting to bring about, the substantial lessening of competition” and would not lose the protection of the solely-for-investment provision.<sup>182</sup>

A second reason for rejecting, in this context, the presumption that an actor intends the likely effects of its actions is that the presumption would render the solely-for-investment provision a nullity. Under Section 7's substantive prohibitions in its first two paragraphs, a stock acquisition or holding that makes a “substantial lessening of competition” likely triggers liability.<sup>183</sup> If “*using*” connotes intentional availment and an investor is taken to intend the likely effects of its stockholding, then at the precise moment a “substantial lessening of competition” becomes probable the investor is “*using* . . . [its stock] to bring about, or in attempting to bring about, the substantial lessening of competition.”<sup>184</sup> If that is so, then at the very moment liability would be triggered under the substantive prohibition of Section 7 (because the investor acquired or held stock when doing

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<sup>181</sup> As economists Daniel P. O'Brien and Keith Waehrer explain, the theory of anticompetitive harm from common ownership

assume[s] that each firm's manager maximizes a weighted sum of the owners' financial returns, which include the owners' earnings through their financial interests in other firms in the same market. The weight that a manager assigns to each owner's profit can be interpreted as a measure of the degree of control or influence the owner has over firm management.

*Id.* at 739.

<sup>182</sup> 15 U.S.C. § 18 (emphasis added).

<sup>183</sup> *Id.*

<sup>184</sup> *Id.*

so would be likely to lessen competition), the investor would lose its protection under the solely-for-investment exemption (because it would be “using . . . [its stock] in [an] attempt[] to bring about . . . [a] “lessening of competition”). And in that case, the solely-for-investment exemption is pointless: it could never insulate anyone from liability, the legal outcome under Section 7 would be the same whether or not the provision was included in the statute, and the provision would be mere surplusage. The better view, then, is that “using” stock “to bring about, or in attempting to bring about, the substantial lessening of competition” requires an actual, not constructive, intent to reduce competition.<sup>185</sup>

### III. SECTION 1 OF THE SHERMAN ACT

Recognizing that “doubts have been raised about whether Clayton Act [Section] 7 can tackle horizontal shareholding . . . because of the solely-for-investment exception,”<sup>186</sup> Professor Elhauge also contends that “horizontal shareholding that has anticompetitive effects can be tackled under the Sherman Act as an ongoing contract or combination that restrains competition.”<sup>187</sup> The basis for liability would be Section 1 of the Sherman Act,<sup>188</sup> which is violated when (1) the defendant enters a “contract, combination in the form of trust or otherwise, or conspiracy” (*i.e.*, an agreement); and (2) that agreement unreasonably restrains trade.<sup>189</sup> Professor Elhauge asserts that if mere common ownership softens competition and thereby reduces market output, it unreasonably restrains trade. In arguing that mere common ownership entails the requisite “contract, combination[,] . . . or conspiracy,” Professor Elhauge offers two theories.<sup>190</sup>

#### *A. The Shareholder Contract Theory*

Professor Elhauge first argues that the agreement element of a Section 1 claim is satisfied by the implicit contract that results from an investor’s stock

<sup>185</sup> *Id.*

<sup>186</sup> Elhauge, *Horizontal Shareholding Harm*, *supra* note 14, at 268.

<sup>187</sup> *Id.*

<sup>188</sup> 15 U.S.C. § 1 (2018) (“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.”).

<sup>189</sup> *Id.* Because most contracts involve a literal “restraint of trade,” the U.S. Supreme Court has interpreted Section 1 of the Sherman Act to forbid only those contracts that *unreasonably* restrain trade by reducing overall market output. *See, e.g.*, *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 U.S. 877, 885 (2007) (observing that “the Court has never taken a literal approach” to Section 1 and has “repeated time and again that [Section] 1 outlaw[s] only unreasonable restraints” (second alteration in original) (first quoting *Texaco Inc. v. Dagher*, 547 U.S. 1, 5 (2006); then quoting *State Oil Co. v. Khan*, 522 U.S. 3, 10 (1997))).

<sup>190</sup> 15 U.S.C. § 1.

purchase (the “shareholder contract”).<sup>191</sup> In buying a corporation’s stock, an investor provides the corporation with capital in exchange for a continuing share of the corporation’s profits and the right to vote on such key decisions as who will direct the company’s business.<sup>192</sup> Although Professor Elhauge concedes that no individual shareholder contract restrains trade, he maintains that the aggregate effect of all an institutional investor’s shareholder contracts in an industry (for example, Vanguard’s shareholder contracts with each separate airline) together with those of other intra-industry diversified investors (for example, the shareholder contracts each airline has with BlackRock, State Street, and Fidelity) is to reduce the incentive of firms within the industry to expand output and reduce prices, resulting in an unreasonable restraint of trade.<sup>193</sup> Professor Elhauge maintains that antitrust tribunals regularly aggregate contract effects this way when assessing the legality of challenged practices.<sup>194</sup> He points specifically to exclusive dealing cases, where the legality of a challenged agreement may turn on the cumulative foreclosure occasioned by all the exclusive dealing contracts in a market, and to resale price maintenance (what Professor Elhauge calls “vertical price-fixing contracts”), where courts consider whether the practice is sufficiently widespread among market participants to facilitate price coordination.<sup>195</sup>

There are two problems with this analysis.<sup>196</sup> First, the implicit contract between a shareholder and the corporation wherein it is invested is not a contract “in restraint of trade or commerce.”<sup>197</sup> The basic shareholder contract does not

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<sup>191</sup> Elhauge, *Horizontal Shareholding Harm*, *supra* note 14, at 269–70. This also seems to be the position espoused by Professors Scott Morton and Hovenkamp, who assert that “the ‘agreement’ requirement [of Section 1] applies to the stock acquisition, not to the subsequent use, and is present whether or not the interest is controlling. The ‘restraint of trade’ standard does not require control, but only that the arrangement serves to reduce output and raise price.” Scott Morton & Hovenkamp, *supra* note 7, at 2035–36. Because a mere acquisition of a non-controlling stock interest would not reduce output, raise prices, or otherwise restrain trade, Professors Scott Morton and Hovenkamp must have in contemplation not simply the purchase of stock, but the implicit shareholder contract resulting from its acquisition.

<sup>192</sup> Elhauge, *Horizontal Shareholding Harm*, *supra* note 14, at 269 (“The ‘contract’ element is clearly met because horizontal shareholding involves formal contracts between corporations and common investors. Those contracts are what give horizontal shareholders rights to vote for corporate management and a share of corporate profits.”).

<sup>193</sup> *Id.* (acknowledging that “each individual shareholder-corporate contract would not, standing alone, restrain competition,” but asserting that “[i]t suffices that the horizontal shareholders have contracts with competing firms and that the effect of the voting and profit rights in those contracts is to lessen competition between those firms”).

<sup>194</sup> *Id.*

<sup>195</sup> *Id.* (“Antitrust has long judged the anticompetitive effects of multiple contracts based on their aggregate impact, such as when it judges exclusive dealing contracts based on cumulative foreclosure or vertical price-fixing contracts based on whether they are sufficiently widespread to facilitate oligopolistic coordination.”).

<sup>196</sup> See *infra* notes 197–210 and accompanying text.

<sup>197</sup> 15 U.S.C. § 1.

prevent or discourage any transactions that otherwise would have occurred. Professor Elhauge attempts to get around this problem by asserting that a trade restraint occurs when all the shareholder contracts of all the investors that are diversified within an industry are aggregated. But antitrust law does not aggregate the effects of non-trade-restraining contracts to produce a restraint of trade. Courts sometimes aggregate the effects of individual trade-restraining contracts—for example, exclusive dealing agreements that restrain one party from trading with others,<sup>198</sup> resale price maintenance agreements that restrain a party from selling a product below a particular price—to determine whether the trade restraint a particular contract effects is unreasonable.<sup>199</sup> They do not, however, aggregate the effects of different parties' non-trade-restraining contracts to produce a trade restraint in the first instance.

More importantly, courts should not treat the basic shareholder contract as a Section 1 agreement because doing so would so drastically expand Section 1's reach that it would undermine a basic principle of antitrust law. Professor Elhauge reasons as follows: (1) ownership of corporate stock involves a contract (*i.e.*, the shareholder agrees to provide capital in exchange for a promise of dividends and the right to vote); (2) intra-industry diversified investors' shareholder contracts, taken together, lead corporate managers to reduce output and raise prices; (3) therefore, an intra-industry diversified investor's shareholder contracts with its portfolio firms are contracts that unreasonably restrain trade in violation of Section 1.<sup>200</sup>

Under this reasoning, every exercise of market power by a for-profit corporation would violate Section 1. A corporation's profits, and thus the dividends paid to its shareholders, grow when the company exercises market power. Professor Elhauge's Section 1 theory of liability would therefore apply any time a corporation exercised market power, because shareholders and corporate managers would have (1) entered contracts that (2) induced the managers to cut back on output to raise profits, and (3) thereby effected an unreasonable restraint of trade. For example, any time a brand name prescription drug manufacturer charged a supracompetitive price for its patented product in an effort to enhance shareholder returns, there would be a contract that unreasonably restrains trade

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<sup>198</sup> See, e.g., *FTC v. Motion Picture Advert. Serv. Co., Inc.*, 344 U.S. 392, 393, 395 (1953) (finding anticompetitive effects because the exclusive dealing agreements of the four firms produced an aggregate foreclosure of 75%); *Standard Oil Co. of Ca. v. United States*, 337 U.S. 293, 295, 309, 314 (1949) (upholding a finding of anticompetitive effects for similar agreements among seven leading oil producers that resulted in an aggregate foreclosure of 65%).

<sup>199</sup> See *Leegin Creative Leather Prods., Inc.*, 551 U.S. at 897 (observing that “[r]esale price maintenance should be subject to more careful scrutiny, by contrast, if many competing manufacturers adopt the practice”).

<sup>200</sup> See Elhauge, *Horizontal Shareholding Harm*, *supra* note 14, at 269–71.

and thus a Section 1 violation.<sup>201</sup> It is a bedrock principle of antitrust law, though, that corporations do not violate the Sherman Act merely by charging supracompetitive prices or otherwise exercising their legitimately obtained market power.<sup>202</sup>

The U.S. Supreme Court has warned against adopting broad interpretations of “contract, combination[.] . . . or conspiracy” that would expand Sherman Act liability in this fashion.<sup>203</sup> In *Copperweld Corp. v. Independence Tube Corp.*, the Court held that there could be no Section 1 agreement between a corporation and its wholly owned subsidiary.<sup>204</sup> The Court emphasized that a robust agreement requirement is necessary to preserve the basic structure of the Sherman Act.<sup>205</sup> The Court observed that Section 1 liability requires something not required for liability under Section 2 (an agreement),<sup>206</sup> while Section 2 includes an element missing from Section 1 (market power).<sup>207</sup> The Court then noted that allowing Section 1’s agreement element to be satisfied by any technical agreement—for example, between a parent and its subsidiary or between multiple officials of a single firm—could cause unilateral firm conduct to violate the Sherman Act under Section 1 even if the acting firm lacked market power so that it could not

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<sup>201</sup> Section 1 of the Sherman Act would also be violated any time a corporation withdrew from a market, or cut back on product features or services some consumers desire, at shareholder behest. Consider the Episcopal Church’s recent campaign to persuade the companies in which it is invested to take actions it believes are morally required. See G. Jeffrey MacDonald, *Investing for an Impact*, THE LIVING CHURCH (Nov. 4, 2019), <https://livingchurch.org/2019/11/04/investing-for-an-impact/> [<https://perma.cc/J4JH-M2NS>]. The denomination purchased stock in gun manufacturers with the hope of inducing corporate managers to eliminate design features that may increase the risk of mass shootings. *Id.* A prominent parish also sought to persuade retail giant Wal-Mart to remove assault weapons from its shelves. See *Trinity Wall St. v. Wal-Mart Stores, Inc.*, 792 F.3d 323, 328–29 (3d Cir. 2015). If these Episcopal shareholders succeed in their efforts either by making a shareholder proposal or setting forth a compelling argument at a shareholder meeting, there would be an unreasonable restraint of trade (a reduction in market output) occasioned by a shareholder contract. Under Professor Elhauge’s view, the ecclesiastical shareholders and the companies responding to their requests would violate Section 1 of the Sherman Act.

<sup>202</sup> See *Pac. Bell Tel. Co. v. Linkline Commc’ns, Inc.*, 555 U.S. 438, 447–48 (2009) (observing that “[s]imply possessing monopoly power and charging monopoly prices does not violate [Sherman Act Section] 2”); *Verizon Commc’ns Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398, 407 (2004) (observing that “[t]he mere possession of monopoly power, and the concomitant charging of monopoly prices, is . . . not unlawful”).

<sup>203</sup> 15 U.S.C. § 1.

<sup>204</sup> *Copperweld Corp. v. Indep. Tube Corp.*, 467 U.S. 752, 771 (1984).

<sup>205</sup> *Id.* at 767–71.

<sup>206</sup> *Id.* at 768 (“Section 1 of the Sherman Act, in contrast, reaches unreasonable restraints of trade effected by a contract, combination[.] . . . or conspiracy between *separate* entities. It does not reach conduct that is wholly unilateral.” (internal quotation marks omitted) (first quoting 15 U.S.C. § 1; then quoting *Albrecht v. Herald Co.*, 390 U.S. 149, 149 (1968), *overruled by State Oil Co.*, 522 U.S. 3 (1977))).

<sup>207</sup> *Id.* at 767 (“The conduct of a single firm is governed by § 2 alone and is unlawful only when it threatens actual monopolization.”).



violate Section 2.<sup>208</sup> The Court reasoned that Section 1's agreement element should not be interpreted so broadly as to disrupt the fundamental structure of the Sherman Act.<sup>209</sup> By the same token, courts should not interpret "contract, combination[,] . . . or conspiracy" in a way that would undermine the long-standing precept that the mere exercise of market power by a corporation is not an antitrust violation.<sup>210</sup>

### *B. The Analogy to Historic Trusts and Holding Companies*

Professor Elhauge also argues that mere common ownership satisfies the agreement element of a Section 1 claim because an investor's ownership of stock of competing companies is a "combination" analogous to the historic trusts (expressly recognized in Section 1 as qualifying combinations),<sup>211</sup> and to illegal holding companies.<sup>212</sup> With the historic trusts, shareholders of competing companies deposited their shares into a trust, allowing them to be collectively managed by the trustee to maximize industry profits.<sup>213</sup> In exchange for their shares, shareholders received trust certificates entitling them to a portion of the trust's profits, which were larger because of the reduced competition among firms within the industry.<sup>214</sup> With illegal holding companies, shareholders of competing firms (the eventual subsidiaries) exchanged their shares for shares of a holding company, which could control the subsidiaries and cause them not to compete, thereby enhancing their aggregate profits.<sup>215</sup> Those profits were then distributed to the holding company's shareholders. According to Professor Elhauge:

[A]ntitrust treatment of both trusts and holding corporations establishes that showing a horizontal agreement or combination does not require proving a direct agreement between two competing firms, but rather can be proven through shareholder contracts between each firm and common horizontal shareholders that indirectly link those two competing firms. Accordingly, when a common set of institutional investors are leading shareholders at competing firms, the shareholder contracts between those firms and their common horizontal share-

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<sup>208</sup> *Id.* at 770–77.

<sup>209</sup> *Id.* at 775 (observing that Congress imposed different requirements for liability under Sections 1 and 2 for "eminently sound reasons" and that "[s]ubjecting a single firm's every action to judicial scrutiny for reasonableness would threaten to discourage the competitive enthusiasm that the antitrust laws seek to promote").

<sup>210</sup> See *supra* note 204 and accompanying text.

<sup>211</sup> 15 U.S.C. § 1 (forbidding every unreasonable "combination in the form of trust or otherwise").

<sup>212</sup> Elhauge, *Horizontal Shareholding Harm*, *supra* note 14, at 269–72.

<sup>213</sup> *Id.*

<sup>214</sup> *Id.*

<sup>215</sup> *Id.* at 269–71.

holders also satisfy the contract or combination requirement of Sherman Act [Section] 1.<sup>216</sup>

This attempt to analogize mere common ownership to the historic trusts and illegal holding companies fails for two reasons. First, both the historic trusts and the holding companies that violated Section 1 involved a combination of *controlling* interests in competing firms. With the trusts, the trustee held all or nearly all of the stock of participating firms and thus combined control of each of them within a single entity.<sup>217</sup> Similarly, the creation of holding companies was condemned under Section 1 when the parent company took a majority interest in multiple competing subsidiaries and thereby gained the ability to control them in a way that would lessen market competition.<sup>218</sup> Combining control of multiple competing firms into a single entity “deprives the marketplace of the independent centers of decisionmaking that competition assumes and demands.”<sup>219</sup> But mere common ownership (as opposed to cross-ownership) involves an investor’s combining of only *non-controlling* interests in competing firms.<sup>220</sup> Accordingly, it does not reduce the number of “independent centers of decisionmaking” in a market the way the historic trusts and illegal holding companies did.<sup>221</sup>

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<sup>216</sup> *Id.* at 270.

<sup>217</sup> See Wayne D. Collins, *Trusts and the Origins of Antitrust Legislation*, 81 *FORDHAM L. REV.* 2279, 2316 (2013) (observing that “[t]he 1882 Standard Oil Trust, which became the model for other trusts . . . was joined by all of the stockholders and members of fourteen corporations and limited partnerships, the controlling stockholders and members of an additional twenty-six corporations and limited partnerships, and forty-six individuals” (footnote omitted)).

<sup>218</sup> See *N. Sec. Co. v. United States*, 193 U.S. 197, 322 (1904) (explaining that the condemned holding company had taken “the capital stock, or a controlling interest in the capital stock, of each of the constituent railway companies”). The Supreme Court also observed that the condemned holding company “ha[d] become the holder—more properly speaking, the custodian—of more than nine-tenths of the stock of the Northern Pacific, and more than three-fourths of the stock of the Great Northern” railroads. *Id.* at 326. Professor Elhauge cites this case to support his position. See Elhauge, *Horizontal Shareholding Harm*, *supra* note 14, at 270 n.310 (citing *id.* 325–27).

<sup>219</sup> *Copperweld Corp.*, 467 U.S. at 769.

<sup>220</sup> See *supra* note 1 and accompanying text.

<sup>221</sup> *Copperweld Corp.*, 467 U.S. at 769. In 1984, in *Copperweld Corp. v. Independence Tube Corp.*, the Court emphasized that:

[I]n any [Section 1] conspiracy, two or more entities that previously pursued their own interests separately are combining to act as one for their common benefit. This not only reduces the diverse directions in which economic power is aimed but suddenly increases the economic power moving in one particular direction.

*Id.* Combining the non-controlling interests of two companies, by contrast, does not preclude those companies from “pursu[ing] their own interests separately,” entail their “combining to act as one for their common benefit,” “reduce[] the diverse directions in which economic power is aimed,” or “increase[] the economic power moving in one particular direction.” *Id.*

Professor Elhauge's analogies also fail because the historic trusts and illegal holding companies, unlike mere common ownership, involved agreements beyond the basic shareholder contract.<sup>222</sup> With the historic trusts, the constituent firms themselves agreed to consolidate using the trust form. As Wayne D. Collins has documented, the firms adopted the trust as their means of combination because the common law at the time would have enforced neither an inter-firm contract to limit competition<sup>223</sup> nor a pooling agreement between the competing firms,<sup>224</sup> and the firms could not simply adopt a unitary ownership structure (for example, some kind of holding corporation) because prevailing corporation law restricted the corporate form in ways that made it unworkable as a combination structure.<sup>225</sup> In addition to these inter-firm agreements, the trusts involved agreements between the shareholders of participant firms: each firm's shareholders agreed to deposit their shares into the trust on the condition that the shareholders of competing firms did the same so that the combined stock could be managed to encourage industry profit maximization.<sup>226</sup> Professor Elhauge is thus wrong when he writes that "the only thing combining the firms [in the historic trusts was] the fact that their shareholder rights [were] held by a common horizontal investor, namely the trust."<sup>227</sup> In fact, firms participating in the trusts were combined by agreements among themselves and among their shareholders.

Holding companies that have been deemed illegal combinations under Section 1 have also involved agreements between the shareholders of different portfolio firms. In the holding company condemned in *Northern Securities, Co. v. United States*, for example, the stockholders of the portfolio railroads collaborated with each other in concocting a scheme to enhance their collective returns.<sup>228</sup>

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<sup>222</sup> As explained above, the implicit contract between a stockholder and the company that it is invested in (i.e., the shareholder's provision of capital in exchange for the promise of dividends and a limited voting right) does not count as a "contract, combination[,] . . . or conspiracy" for purposes of Section 1. 15 U.S.C. § 1; see *supra* notes 192–210 and accompanying text.

<sup>223</sup> Collins, *supra* note 217, at 2293–2307.

<sup>224</sup> *Id.* at 2307–09.

<sup>225</sup> *Id.* at 2309–15.

<sup>226</sup> *Id.* at 2316 (observing that "[t]he 1882 agreement [creating the Standard Oil trust] was joined by all of the stockholders and members of fourteen corporations and limited partnerships, the controlling stockholders and members of an additional twenty-six corporations and limited partnerships, and forty-six individuals, all of whom would be the beneficiaries of the trust").

<sup>227</sup> Elhauge, *Horizontal Shareholding Harm*, *supra* note 14, at 270. Professor Elhauge is also wrong in stating that "antitrust treatment of . . . trusts . . . establishes that showing a horizontal agreement or combination does not require proving a direct agreement between two competing firms." *Id.* There were agreements between the rival firms in the trusts.

<sup>228</sup> *N. Sec. Co.*, 193 U.S. at 326. The Court explained:

[I]t is indisputable upon this record that . . . the stockholders of the Great Northern and Northern Pacific Railway corporations, having competing and substantially parallel lines[,] . . . combined and conceived the scheme of organizing a corporation under the laws of New Jersey, which should hold the shares of the stock of the constituent com-

With mere common ownership, there are no agreements between the competing portfolio firms (as with the historic trusts) or between the shareholders of different competing firms (as with both the trusts and the holding companies whose creation violated Section 1). Take, for example, the airline industry. Even if institutional investors' common ownership of airlines has lessened market competition (a point not conceded here),<sup>229</sup> there is no evidence that the airlines have agreed to act in concert or to pursue a common ownership structure (as the firms in the historic trusts did), or that the institutional investors holding stock in multiple airlines have agreed to press the companies to reduce competition among themselves (as did the shareholders of firms in the trusts and in illegal holding companies). The only "agreements" among the individuals and entities in the airline industry are the basic shareholder agreements between investors and each of their portfolio firms, which, for reasons set forth above, are not cognizable Section 1 agreements.<sup>230</sup> Rather, they are intra-enterprise agreements between capital providers and managers.

Proponents of imposing Section 1 liability on the basis of mere common ownership may respond that, even when intra-industry diversified institutional investors do not hold controlling shares of their portfolio firms, they still exercise de facto control over those firms because firm managers defer to the interests of their largest shareholders, all of which are intra-industry diversified.<sup>231</sup> Thus, common ownership results in a combination of *effective* controlling interests in competing companies, just as the historic trusts and illegal holding companies combined controlling stakes of separate rivals.

The problem with this reasoning is that mere common ownership does not amalgamate de facto controlling interests *within any single entity or group of collaborating entities*. No single institutional investor combines de facto controlling interests, for the common ownership literature asserts that a softening of

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panies, such shareholders, in lieu of their shares in those companies, to receive, upon an agreed basis of value, shares in the holding corporation; that pursuant to such combination the Northern Securities Company was organized as the holding corporation through which the scheme should be executed; and under that scheme such holding corporation has become the holder—more properly speaking, the custodian—of more than nine-tenths of the stock of the Northern Pacific, and more than three-fourths of the stock of the Great Northern, the stockholders of the companies who delivered their stock receiving *upon the agreed basis* shares of stock in the holding corporation.

*Id.* (first and third emphasis added).

<sup>229</sup> See Lambert & Sykuta, *supra* note 29, at 233–48 (criticizing the theory and evidence of anti-competitive harm from common ownership).

<sup>230</sup> See *supra* Part III.A. and accompanying text.

<sup>231</sup> See, e.g., Posner et al., *Proposal*, *supra* note 6, at 684–85 (“[S]omeone must determine the firms’ goals. That controller is likely to be one of the largest shareholders. If there are no large concentrated shareholders, then the firm will likely be run in the interests of its institutional investors even if these do not individually own very large stakes.”).

competition results from the overall pattern of stock ownership among all the investors in the industry—for example, from the fact that multiple large investors are intra-industry diversified and there are no shareholders holding large blocks of single firms within the industry.<sup>232</sup> It is no answer to say that intra-industry diversified institutional investors *as a group* have combined de facto controlling interests because there is no evidence of any agreement among institutional investors to work together as a group in managing the stock that they collectively own.<sup>233</sup>

Proponents of Section 1 liability may retort that the absence of any such agreement is inconsequential because intra-industry diversified institutional investors act in parallel to pursue industry profit maximization and a lessening of market competition. But it is well-established in antitrust law that mere parallel conduct cannot establish an agreement for purposes of Section 1 when each individual firm has an incentive to act as it does, regardless of what the other firms do.<sup>234</sup> This principle would apply to intra-industry diversified institutional investors. Parallel conduct cannot establish a Section 1 agreement absent a “conscious commitment to a common scheme designed to achieve an unlawful objective.”<sup>235</sup> There is no evidence that institutional investors have consciously committed to act in concert in causing their portfolio firms to pursue industry profit maximization. Accordingly, there is no “group” of institutional investors who have collectively combined de facto controlling interests in competing firms.

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<sup>232</sup> See *id.* at 683–84 (explaining logic of MHHIA, which purports to measure competition-lessening incentives resulting from overall pattern of ownership in an industry). Even with significant common ownership by multiple investors, the holding of large blocks by investors who are not intra-industry diversified will, according to the theory, prevent competition-softening. *Id.* at 684 (discussing effect of blockholders).

<sup>233</sup> Professor Elhauge appears to have in mind a combination of interests within such a group of shareholders when he writes that “a horizontal agreement or combination . . . can be proven through shareholder contracts between each firm and *common horizontal shareholders* that indirectly link those . . . competing firms.” Elhauge, *Horizontal Shareholding Harm*, *supra* note 14, at 270 (emphasis added). He further asserts that “when a *common set of institutional investors* are leading shareholders at competing firms, the shareholder contracts between those firms and their common horizontal shareholders also satisfy the contract or combination requirement of Sherman Act [Section] 1.” *Id.* (emphasis added).

<sup>234</sup> *Compare* *Theatre Enters., Inc. v. Paramount Film Distrib. Corp.*, 346 U.S. 537, 542–43 (1954) (holding that the parallel conduct did not establish agreement where each firm had independent incentive to act as it did, regardless of competitors’ actions), *with* *Interstate Circuit, Inc. v. United States*, 306 U.S. 208, 221–27 (1939) (holding that the agreement could be inferred from consciously parallel conduct that would have been economically irrational if engaged in unilaterally).

<sup>235</sup> *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 764 (1984) (quoting *Edward J. Sweeney & Sons, Inc. v. Texaco, Inc.*, 637 F.2d 105, 111 (3d Cir. 1980)).

#### IV. WHY ANTITRUST CONDEMNATION OF MERE COMMON OWNERSHIP WOULD LIKELY REDUCE SOCIAL WELFARE

Thus far, this Article's analysis has been legal and descriptive: it has shown why neither Section 7 of the Clayton Act nor Section 1 of the Sherman Act condemn mere common ownership. Next, this Article considers why, as a normative matter, that is a good thing. In short, those who call for condemning mere common ownership under the antitrust laws have not shown that the marginal benefits of such condemnation are likely to exceed the marginal costs it would entail. Courts and enforcers should thus refrain, at least on the current record, from adopting aggressive interpretations of Section 7 of the Clayton Act and Section 1 of the Sherman Act to preclude mere common ownership.

The marginal benefit of condemning mere common ownership would be the elimination of anticompetitive harms (*i.e.*, allocative inefficiencies from supracompetitive pricing) that result from the practice. On the current record, we have no idea of the magnitude of those harms and thus of the benefit of eliminating them. To be sure, the studies purporting to show harms from common ownership have estimated adverse price effects of the practice. The airline study, for example, concluded that airfares are 3% to 7% higher because of current levels of common ownership.<sup>236</sup> Likewise, the banking study found that a one standard deviation increase in the common ownership metric raised fees on interest-bearing checking accounts by 11% and increased the minimum balance required to avoid fees by 17%.<sup>237</sup> The trustworthiness of those studies, however, is a matter of dispute as they have been criticized on methodological grounds,<sup>238</sup> and other studies have reached contrary conclusions.<sup>239</sup>

More importantly for our purposes, the studies have not attempted to quantify the adverse effects of *mere* common ownership, and they therefore tell us nothing about the marginal benefit of expanding the scope of the antitrust laws to condemn it. As explained above, the studies that purport to show harm from horizontal shareholding correlate some measure of common ownership of the firms in a market—MHHA or a variant thereof—with price effects in that market.<sup>240</sup> In so doing, the studies have lumped together all instances of common ownership: those accompanied by anticompetitive agreements (for example, hub-and-spoke conspiracies, collaborations among common investors to encourage industry profit maximization), and those where no such agreements are present. This is understandable, as it would be extremely difficult for researchers to know

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<sup>236</sup> See *supra* notes 38–40 and accompanying text.

<sup>237</sup> See *supra* notes 41–45 and accompanying text.

<sup>238</sup> See *supra* note 46 and accompanying text.

<sup>239</sup> See *supra* note 47 and accompanying text.

<sup>240</sup> See *supra* notes 31–45 and accompanying text.

when common ownership involved additional anticompetitive agreements and when it did not. But the failure to segregate instances of mere common ownership from “common ownership plus anticompetitive agreement” implies that the common ownership studies cannot give a sense of the added social benefit that would result from policing the former. It could be that most of the alleged welfare loss from common ownership could be eliminated simply by stepping up enforcement against anticompetitive agreements that may emerge when there is substantial common ownership of firms in concentrated industries. If that is the case, the marginal benefits of expanding antitrust to condemn *mere* common ownership could be small.

In any event, the efficiency gain from eliminating the slight price increases allegedly shown to result from common ownership is the *upper limit* of the potential marginal benefit from condemning mere common ownership. If critics are correct that the common ownership studies have overstated the social harms of horizontal shareholding, or if such harms could be reduced by simply stepping up enforcement against actual anticompetitive agreements (common ownership “plus”), then the marginal benefits of condemning mere common ownership will be less than the quantum of harm purportedly demonstrated by the common ownership studies.

Although it is unclear whether condemning mere common ownership would secure significant marginal benefits, it would almost certainly entail substantial marginal costs. Assuming that institutional investors continue to hold stocks of multiple firms competing in concentrated markets, there would be the costs of deciding whether an instance of common ownership violates the law. Such “decision costs” would be borne by enforcers in deciding whether to challenge instances of common ownership, by adjudicators in determining whether to assign liability, and by business planners in determining whether the conduct under consideration is legally permitted. For all three groups, the decision costs of a rule condemning mere common ownership would be significant.

To see why, consider the likely circumstances wherein mere common ownership would be condemned. Because many instances of the practice entail no competitive threat, *per se* condemnation would be inappropriate,<sup>241</sup> and antitrust liability would presumably attach only where product market concentration and the overall pattern of ownership of the stock of firms participating in the market indicate that anticompetitive harm is plausible.<sup>242</sup> Professor Elhauge has pro-

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<sup>241</sup> See *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 U.S. 877, 886 (2007) (“Resort to *per se* rules is confined to restraints, like those mentioned, ‘that would always or almost always tend to restrict competition and decrease output.’” (quoting *Bus. Elecs. Corp. v. Sharp Elecs. Corp.*, 485 U.S. 717, 723 (1988))).

<sup>242</sup> In unconcentrated, highly competitive markets, horizontal shareholding would be unlikely to occasion anticompetitive harm. And, even in concentrated product markets, larger investments by

posed to implement such a screen using MHHI.<sup>243</sup> Specifically, he contends that the federal antitrust agencies “should investigate any horizontal stock acquisitions that have created, or would create, a MHHIΔ of over 200 in a market with an MHHI over 2500, in order to determine whether those horizontal stock acquisitions raised prices or are likely to do so.”<sup>244</sup> Liability would thus result where (1) common ownership has led to MHHI and MHHIΔ levels in excess of 2500 and 200, respectively; and (2) there are indications that common ownership has had, or threatens, an adverse price effect in the market.

The decision costs facing enforcers and adjudicators under this approach would be substantial.<sup>245</sup> To determine whether the MHHI-based thresholds were met, they would have to define the markets where firms with common shareholders compete and calculate MHHI and MHHIΔ for each. If the thresholds were exceeded, they would have to assess complicated econometric evidence and resolve inevitable battles among experts to determine whether and to what extent common ownership had raised or was likely to raise prices. Adjudicators would then confront the difficult matter of allocating liability among the investors holding stakes in multiple firms competing in the market. One approach would be to assign liability only to those intra-industry diversified investors that could substantially reduce MHHIΔ by divesting from the market. Such an approach often would not work, however, for in many situations each individual investor’s unilateral divestment would reduce MHHIΔ by only a slight amount.<sup>246</sup> An alternative approach would be to impose joint liability on all investors holding stakes in multiple firms within the market. It is likely, though, that the investor(s) from whom a plaintiff actually collected would seek contribution from other intra-industry diversified investors, and it would seem inequitable not to permit such actions. In the end, then, courts would have to find some way to address the intractable question of how to allocate any economic harm from common ownership among investors holding stakes in multiple competitors within the market.

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undiversified blockholders (who have an interest in own-firm profit maximization) would tend to preclude anticompetitive harm resulting from smaller holdings by intra-industry diversified investors. See Posner et al., *Proposal*, *supra* note 6, at 684 (explaining how presence of single-firm blockholders reduces managers’ incentives to lessen competition).

<sup>243</sup> Elhauge, *Horizontal Shareholding*, *supra* note 5, at 1303.

<sup>244</sup> *Id.* Professor Elhauge would also allow private treble damages actions when those requirements are met. For example, “[a] class of passengers injured by paying higher airline fares because of horizontal shareholdings on a concentrated route could . . . bring suit on the theory that the stock acquisitions by institutional investors that created those horizontal shareholdings harmed the passengers by lessening airline competition.” *Id.* at 1304.

<sup>245</sup> See Lambert & Sykuta, *supra* note 29, at 250–53 (detailing the decision costs for adjudicators and enforcers in MHHIΔ-based lawsuits).

<sup>246</sup> See Posner et al., *Proposal*, *supra* note 6, at 692–93 (offering an example to illustrate that unilateral divestment may have little effect on MHHIΔ).



As great as the decision costs would be for enforcers and adjudicators, those facing business planners would be larger still.<sup>247</sup> Given that no single institutional investor could prevent the adverse price effects that would satisfy the second element of Professor Elhauge's liability test, institutional investors could protect themselves from liability only by negating the first, which would require them to refrain from common ownership in markets where MHHI and MHHIA exceed certain levels. That would require business planners to calculate and continually monitor MHHI and MHHIA in every market where their institutions held stock of multiple competitors. Because both metrics are influenced by (1) the market shares of the firms sharing common owners, (2) the ownership percentages of the firms' common shareholders, and (3) the ownership stakes of the firms' non-diversified shareholders, an institutional investor holding shares of competing firms could find itself at risk of antitrust liability if the market shares of its portfolio firms rose, if other intra-industry diversified investors adjusted their holdings of firms within the industry, or if major non-diversified shareholders decreased their ownership stakes.<sup>248</sup> Planners for an institutional investor holding stakes in competing firms would therefore have to recalculate MHHI and MHHIA on a near daily basis to ensure that the investor's stockholding—the one thing the investor can control—could not be deemed to have contributed to a softening of competition.

Of course, institutional investors could avoid these decision costs if they simply refrained from holding shares of multiple firms competing in concentrated markets.<sup>249</sup> That appears to be the outcome that Professor Elhauge and other common ownership critics seek to encourage with their proposals to impose antitrust liability based on mere common ownership.<sup>250</sup> But, if institutional investors were to take that tack, retail investors would lose access to many of the diversified investment opportunities that create value for them.<sup>251</sup>

Most obviously, driving institutional investors to refrain from intra-industry diversification would eliminate true index funds. Nearly all significant stock in-

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<sup>247</sup> See Lambert & Sykuta, *supra* note 29, at 253–55 (discussing business planners' decision costs under Professor Elhauge's proposed MHHIA-based liability rule).

<sup>248</sup> See *supra* notes 32–37 and accompanying text. See generally Lambert & Sykuta, *supra* note 29, at 271–78 (providing “A Non-Technical Guide to Calculating MHHIA”).

<sup>249</sup> And if institutional investors eschewed common ownership, antitrust enforcers and courts would not need to incur the decision costs described above. See *supra* notes 247–248 and accompanying text.

<sup>250</sup> See Elhauge, *Horizontal Shareholding*, *supra* note 5, at 1314 (“When investing in horizontal competitors would create significant horizontal shareholdings in a concentrated market, investors can avoid antitrust liability by investing in only one of the competing firms.”); Posner et al., *Proposal*, *supra* note 6, at 714 (“Our proposal will encourage large institutional investors to shift holdings so that they have larger stakes in individual firms—for example, a large stake in GM rather than smaller stakes in GM, Ford, and Chrysler.”).

<sup>251</sup> See Lambert & Sykuta, *supra* note 29, at 263–64.

dexes include more than one firm from some concentrated industry, so fund managers could not simply invest in all the firms included in an index. Although they could select one indexed firm from each concentrated industry, any fund that was so managed would not be a true index fund; a hallmark of such a fund is the absence of manager discretion, resulting in lower management fees.<sup>252</sup>

Inducing each institutional investor to hold stock in only one firm per concentrated industry would also reduce the variety of actively managed mutual funds that retail investors could select.<sup>253</sup> Common ownership critics maintain that intra-industry diversification *at the institutional investor level*—not just at the individual fund level—leads to softened competition in concentrated markets.<sup>254</sup> That implies that institutional investors could not avoid liability for common ownership merely by ensuring that each of their individual funds held stock in only one firm competing in a concentrated industry. Each institutional investor would instead have to select only one company per concentrated industry *for all of its individual funds*. Thus, institutional investors could not offer a diverse range of actively managed mutual funds featuring different investment strategies such growth, income, or value. As an example, if Southwest Airlines was a growth stock and United Airlines a value stock,<sup>255</sup> an institutional investor would be unable to offer a growth fund featuring Southwest and a value fund featuring United.

Eschewing intra-industry diversification would also make it impossible for institutional investors to design funds that bet on an industry as a whole but limited fund investors' exposure to company-specific risks within that industry.<sup>256</sup> Imagine, for example, a financial crisis that led to a sharp, across-the-board decline in the stock prices of commercial banks. A retail investor might believe that the commercial banking sector as a whole would rebound but that some individual banks would likely fail. That investor would want to invest in commercial

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<sup>252</sup> See Alicia Adamczyk, *Index Funds Are More Popular Than Ever—Here's Why They're a Smart Investment*, CNBC (Sept. 19, 2019), <https://www.cnbc.com/2019/09/19/why-index-funds-are-a-smart-investment.html> [<https://perma.cc/5D6F-4VZD>] (observing that “because you’re not paying someone to pick stocks for you anymore, index funds tend to be less expensive for investors than actively managed funds”).

<sup>253</sup> See Lambert & Sykuta, *supra* note 29, at 263.

<sup>254</sup> The airline and banking studies examine common ownership at the institutional investor level, not at the fund level. See Azar et al., *Anticompetitive Effects*, *supra* note 31, at 1523–25; Azar et al., *Ultimate Ownership*, *supra* note 41, at 7–8; Lambert & Sykuta, *supra* note 29, at 238.

<sup>255</sup> A “growth stock” is a stock that grows more quickly than the prevailing rate of stocks in the market, typically with high price to equity ratios and high earnings per share. *What Are Growth Stocks vs Value Stocks?*, CFI, <https://corporatefinanceinstitute.com/resources/knowledge/trading-investing/growth-stocks-vs-value-stocks/> [<https://perma.cc/WA3W-BLAK>] (defining a “value stock” as a stock that is traded at a discount from its intrinsic value, most often the stock in a large entity that is currently undervalued but is likely to regain value over time). *Id.*

<sup>256</sup> See Lambert & Sykuta, *supra* note 29, at 263–64.

banking generally but to limit risk by holding a diversified portfolio within the sector. If institutional investors were induced to hold only one stock per industry, they could not offer the sort of fund this retail investor would prefer.

The welfare squandered by eliminating these sorts of value-creating investment opportunities would constitute “error costs”—*i.e.*, losses that result from discouraging welfare-enhancing practices in the quest to preclude welfare-reducing ones.<sup>257</sup> Other error costs would emerge if institutional investors sought to avoid antitrust liability by remaining entirely passive—not voting their shares, engaging with management, or threatening to sell their shares—at the firms where they are invested. They might take such a tack so that they could claim they had no influence over their portfolio firms, and thus could not have contributed to any softening of competition.<sup>258</sup> But, such passivity by institutional investors creates its own costs: empirical evidence shows that long-term institutional investors tend to reduce agency costs at their portfolio firms,<sup>259</sup> and those efficiencies would likely not be achievable if institutional investors were fully passive.<sup>260</sup>

In the end, then, condemning mere common ownership is likely to generate significant costs, either in the form of decision costs (if institutional investors continue to invest in competing firms and to vote their shares), error costs (if such investors respond to potential liability by refraining from intra-industry diversification or remaining fully passive at their portfolio firms), or both. It hardly seems wise to embrace a liability rule that would generate these predictable costs to achieve only speculative marginal benefits.

## CONCLUSION

Mere common ownership—horizontal shareholding involving no effort to coordinate portfolio firms’ behavior or exercise management control and no ownership of control-conferring stakes—does not violate the U.S. antitrust laws.

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<sup>257</sup> See THOMAS A. LAMBERT, *HOW TO REGULATE: A GUIDE FOR POLICYMAKERS* 10 (2018) (defining “error costs”). The losses here would be Type I error costs—welfare reductions from wrongly condemning efficient conduct. The welfare losses from failing to prevent anticompetitive instances of common ownership would be Type II error costs. The discussion in the text treats avoidance of Type II error costs as a marginal benefit of condemning mere common ownership.

<sup>258</sup> Cf. Posner et al., *Proposal, supra* note 6, at 712 (proposing an antitrust safe harbor for intra-industry diversified institutional investors who remain purely passive, as described).

<sup>259</sup> See generally Jarrad Harford, Ambrus Kecskés & Sattar Mansi, *Do Long-Term Investors Improve Corporate Decision Making?*, 50 J. CORP. FIN. 424 (2018) (examining large panel of firm year comprising around 3,000 firms annually over a near thirty-year period). Jarrad Harford, Ambrus Kecskés, and Sattar Mansi concluded that long-term investment by active institutional investors enhanced quality of corporate management, reduced measurable instances of managerial misbehavior, boosted innovation, decreased debt maturity (causing firms to become more exposed to financial market discipline), and increased shareholder returns. *Id.*

<sup>260</sup> See Lambert & Sykuta, *supra* note 29, at 264–69.

Such ownership is immune from liability under Section 7 of the Clayton Act because of the solely-for-investment exemption. It does not violate Section 1 of the Sherman Act because it does not involve the sort of contract, combination, or conspiracy that is required for liability under that provision.

This is a good thing. Condemning mere common ownership under Section 7 or Section 1 would either deny investors access to valuable investment products (if institutional investors were to forego intra-industry diversification) or increase corporate agency costs (if institutional investors opted to continue intra-industry diversification but remain completely passive in the industries that they were diversified in). In contrast to these likely and significant marginal costs, the marginal benefits of condemning mere common ownership are, on the current empirical record, speculative. The studies purporting to show anticompetitive harm from common ownership suffer from methodological difficulties, and subsequent studies contradict them. Because they fail to segregate mere common ownership from instances of common ownership accompanied by anticompetitive agreements, they likely overstate the harms from, and thus the benefits of prohibiting, common ownership simpliciter. On the current empirical record, then, courts and antitrust enforcers should resist calls to expand the prohibitions of Sections 7 and 1 to condemn mere common ownership.

