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Antitrust Law

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SIGNIFICANT LAW REVIEW ARTICLES

ANTITRUST LAW

SECTION 7 OF THE CLAYTON ACT AND THE MERGING OF LAW AND ECONOMICS, by Derek C. Bok, 74 Harv. L. Rev. 226 (December 1960).

The purpose of Professor Bok's article is to suggest ways in which law and economics might make common cause in determining how Section 7 can best be applied to mergers between competing firms. His exhaustive research on the problem leads him not only to a study of the legislative history of the Act but also into an examination of current economic theory on the effects of merger. He argues that the present approaches to the construction of Section 7 are inadequate and concludes that the interpretation of that section must be based, in particular contexts, upon a single significant factor as the standard of legality.

Section 7 of the Clayton Act, as amended, forbids any corporation from absorbing all or any part of another company "where the effect thereof may be substantially to lessen competition or to tend to create a monopoly." The Supreme Court of the United States has not yet had serious occasion to consider a test which can validly be used in the application of that Section. The legislative history of the Act is chiefly important for the common values and apprehensions which were expressed by so many who stood for the bill. As a practical guide, however, it fails to yield much concrete assistance beyond an occasional suggestion of rather vague dimensions. Professor Bok, attempting to find some solutions in terms of economic theory, considers studies based both upon empirical knowledge and theoretical analysis.

He found that these studies fall short of revealing the consequence of many mergers. He finds no theoretical treatment which suggests that factors, such as the importance or strategic value of the commodity produced, the number of men employed, the total assets of the corporation, etc., could be woven together into a consistent whole. There has been no method suggested for integrating these factors into an economic theory in a manner susceptible of systematic legal application under a statute concerned with all the varying consequences of mergers.

Finding no assistance in either the legislative history or economic theory, Professor Bok discusses the three different constructions of Section 7 which have been advanced:

1. The approach of the Government, that is, the quantitative substantiality doctrine. Transplanted into Section 7, the quantitative substantiality doctrine would seemingly imply that any horizontal merger could be struck down on a showing that the acquired firm sold a substantial share—perhaps some six to seven percent—of goods in the relevant market.
2. The approach of the defendant. Under this interpretation of

Section 7, the result would be in favor of the defendant in any case in which the probable consequences of a merger cannot be ascertained, on the ground that the Government has simply failed to meet its burden of proof. The essence of this approach lies in an attempt to capitalize upon the defects in our present knowledge about mergers.

3. The approach of the Attorney General's Committee. This approach, which supposedly is the position of the "expert," recoils from any conceptual grossness of the quantitative substantiality doctrine, at least where the market share of the acquired firm is not extremely large. Instead, a flexible approach is recommended in which "different factors may be equally important" and no one pattern of proof can meet the requirements of all cases. Factors which might be considered are "long-run supply and demand picture," "the incentive of sellers or potential sellers to enter new markets and to improve their products or services," "adjustment by other companies to the actual and expected shifts in markets affected" and the "opportunities for innovation in products . . . or methods of sale." The striking aspect of this approach is that there is a lack of any suggestion as to the manner in which these factors may be applied in any given case.

The author shows how each one of these tests fails to achieve its goal and, in fact, impedes effectuation of congressional policy. He argues that there is much to be said for a single significant factor which can at least be fairly and inexpensively administered in a fashion that is understandable to the businessman contemplating merger. This most meaningful single factor in appraising a merger by the largest firm is the extent to which that merger has increased the superiority in the leader's size beyond the margin of superiority enjoyed during a base period prior to the merger. The author develops this theme fully, showing when additional factors might have to be taken into account and when an exception would have to be carved out.

The situation most commonly arising under Section 7 is that of an acquisition by a firm that is not the largest but only one of the largest companies in the market. Professor Bok argues that the most logical test to employ would be one based upon increases in concentration. The court or agency should look to the change that has taken place in the aggregate share possessed by the largest firms in the market. The number of firms selected for this purpose should be large enough to include the acquiring firm but should not be unreasonably large (more than eight firms). The merger should then be disallowed if the aggregate share following the acquisition substantially exceeds (by seven or eight percentage points or more) the aggregate share of the market controlled by the same number of firms at any time during a period reasonably (five to ten years) prior to the acquisition. The author concludes his article with a discussion of other factors which have been suggested for use in cases arising under Section 7:

1. The nature of competition in the market.
2. Growth and other dynamic factors.

3. Vertical effects of the merger.
4. Competitive advantages of the merging firms.
5. Prior acquisitions by the merging firms.

A separate section is devoted to the failing company defense.

The value of Professor Bok's article rests upon his successful attempt to fuse law and economic theory in order to achieve an intelligible standard with which to construe Section 7 of the Clayton Act.

THEODORE C. REGNANTE

CORPORATIONS

DUTIES OF DISCLOSURE OF CORPORATE INSIDERS WHO PURCHASE SHARES, by Michael Conant, 46 Cornell L.Q. 53 (Fall 1960).

Professor Conant examines the question of whether a corporate officer or director who purchases outstanding shares in his firm has an affirmative fiduciary duty of disclosure to the selling shareholder. The factual basis of the corporate insiders fiduciary duties to his corporation and the arguments for extending the duty of disclosure to the individual shareholder are discussed and analyzed, as is the impact of Federal legislation in this area. Specific legislation is recommended since the traditional remedies of the courts will not suffice to solve the problem.

The majority of decisions have held that there is no fiduciary duty upon the insider to make affirmative disclosures to individual shareholders of facts which may affect the value of the stock, obtained by virtue of his position with the company, in the absence of actual fraud. Since the insider is not dealing with the corpus of his trust, the corporate management, property and business opportunities, the courts see no reason for extending the fiduciary duty to the individual shareholder. The law of fraud demands honest and complete answers to questions asked by the seller, but the burden of disclosing the facts should not rest on the insider absent inquiry.

The minority-rule courts hold that the insider is a fiduciary of each individual stockholder and must disclose all material or special circumstances within his knowledge that might have a bearing on the value of the stock, and are not readily available in the corporations books or financial reports. Most of the cases decided by these courts could have been founded on common law fraud or a duty of trust arising from another source. The author maintains that insiders should be held to account to the corporation for all profit gained through use of corporate information but that this remedy cannot be extended to the individual shareholder on a theory sounding in trust.

Section 16B of the Securities Exchange Act of 1934 bolsters the author's contention that the fiduciary duty of the corporate insider is owed to the