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COMPETITION, CONTRACT, AND VERTICAL INTEGRATION

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Vertical integration, the coordination of successive stages of production or distribution, has received considerable attention in recent years. This attention, however, has been confined largely to integration by stock or asset acquisition—ownership integration. Contract integration—vertical contractual arrangements such as requirement, output, exclusive dealing, franchise, consignment, and agency agreements—has just begun to be treated as a form of vertical integration although it is widely used to achieve industrial coordina-

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The authors wish to thank Mrs. Jonathan Fine of the Massachusetts Bar for valuable assistance in research; our greatest debt is to Ward S. Bowman, Jr., Professor of Law and Economics at the Yale Law School, who gave us the benefit of his great learning and creative perception with unsurpassed generosity and cordiality of spirit.

1. Cole defines "vertical integration" as "that type of organization that comes into existence when two or more successive stages of production and/or distribution are combined under the same control." Cole, General Discussion of Vertical Integration, in Vertical Integration in Marketing 9, 99 (Bureau Econ. & Bus. Research, U. Ill., No. 74, 1952). According to Adelman, "a firm is called vertically integrated when it transmits from one of its departments to another a good or service which could, without major adaptation, be sold in the market." Adelman, Integration and Antitrust Policy, 63 Harv. L. Rev. 27 (1949); Bork adopts this definition in Vertical Integration and the Sherman Act: The Legal History of an Economic Misconception, 22 U. Chi. L. Rev. 157 n.1 (1954). For Frank, "[V]ertical Integration may be described as the functional co-ordination of one or more units in each of the several successive stages of production, so that they are all operated as a single, unified industrial process." Frank, The Significance of Industrial Integration, 33 J. Pol. Econ. 179 (1925). See also Burns, The Decline of Competition 421 (1936) (salability of intermediate products).

2. The vertical joint-venture agreement might be added to this list of contractual coordination devices. Joint venture is a hybrid integration device which combines ownership and contract. Typically, a supplier and his customer set up a jointly owned subsidiary in order to transact their business. See note 14 infra.

3. See McLaren, Related Problems of "Requirements" Contracts and Acquisitions in Vertical Integration Under the Anti-Trust Laws, 45 Ill. L. Rev. 141 (1950); Adelman, Corporate Integration, in How To Comply With the Antitrust Laws 200, 303-04 (Van Cise & Dunn ed. 1954); Rostow, Over All Size, in id. 311, 323; HALE & HALE,
tion and even control. Nor have informal understandings which are ancillary to formal contracts and which aim at coordination have been included in an overall concept of integration.

As a result, the functional similarities or differences between these alternative methods of integration have been underemphasized or ignored. Contractual arrangements aimed at coordinating the supply of materials or disposal of output frequently affect the contracting firms, as well as the rest of the industry, in much the same way as ownership of suppliers or outlets does. But important differences may attend the two devices—differences in business effectiveness and in legal consequences. With an eye toward possible differences between ownership and contract, part I of this Article will deal with the industrial and economic aspects of vertical integration. The remaining parts are devoted to legal problems: part II examines the effect of the antitrust laws on integration systems and part III considers the impact of pricing regulations.

I. VERTICAL INTEGRATION IN ITS BUSINESS SETTING

The Impact on the Firm

Cost reduction is the principal technological justification for vertical integration. "Cost reduction," however, is a broad term which requires further

Market Power: Size and Shape Under the Sherman Act 204 (1958) ("vertical control"). Compare id. n.12 (§ 3 of the Clayton Act not applicable); Levi, The DuPont Case and § 7, 3 Antitrust Bull. 1, 10 (1958). However, the courts have been aware that contractual arrangements may serve as alternatives to ownership integration. See Standard Oil Co. v. United States, 337 U.S. 293, 319 (1949) (dissenting opinion of Douglas, J.); cf. Mandeville Island Farms, Inc. v. American Crystal Sugar Co., 334 U.S. 219, 243-44 (1948); Gulf Ref. Co. v. Fox, 297 U.S. 381 (1936).

Contractual arrangements aiming at vertical integration extend over a wide range, verging at one extreme on the permanence and control of ownership integration, and at the other approaching the impermanence and lack of control of the spot-market transaction.

4. For example, manufacturers frequently have an understanding of exclusive dealing with their dealers, although exclusive dealing is not required by the formal sales contract. This is particularly common when the manufacturer leases the premises to the dealer.


5. Adelman, Integration and Antitrust Policy, 63 Harv. L. Rev. 27, 48 (1949) ("Successful integration . . . consists in the saving of overhead, and results in doing a given job more cheaply.").

Of course, vertical integration may occur without any rational justification. Historical accident and mere chance may cause a vertical integration pattern in an industry where there are no economies or diseconomies of scale. Adelman, Concept and Statistical
analysis, for it encompasses a multitude of reasons for adopting integration. Perhaps the most important of these is the increased stability of operations that coordination affords. Consumer outlets, sources of supply, and uniformity of quality are made more secure, thus increasing the feasibility of long-range planning. Facilities can be fully utilized, overtime production or idle plant minimized, and inventory reduced. Moreover, vertical integration eliminates many costs incurred in the transfer of goods from one control to another. The most obvious of these are marketing expenses. Also, when goods are manufactured for general salability rather than for a specific known function, many all-purpose features unnecessary to each individual buyer are incorporated, thereby raising the cost of production in order to increase market appeal. Such “functional cross-hauling” costs can be eliminated by integration.


6. For example, to the extent that vertical integration lessens human wear and tear attendant to the constant making of sales contracts, it is a cost reduction factor. See Llewellyn’s excellent discussion of this point in Book Review, 52 Harv. L. Rev. 700, 701 (1939), referring to the human economics of standardized contracts.

7. See Dean, Managerial Economics 117 (1951); Girdner, Integrated Marketing Institutions, 209 Annals 55 (1940). In Goodyear Tire & Rubber Co., 22 F.T.C. 232, 287 (1936), respondent defended itself against a charge of violation of § 2 of the Clayton Act by asserting that the large assured volume obtained from its requirements contract integration with Sears, Roebuck served to “remove hazards and insure stability by avoiding the fluctuation of profit inevitable in respondent’s other business . . . .” See note 526 infra.


8. This factor is most significant when overhead costs are large. See Davis, Vertical Integration in the Textile Industries 3 (1938).

9. Kimball & Kimball, op. cit. supra note 7, at 61; Frank, The Significance of Industrial Integration, 33 J. Pol. Econ. 179, 190-91 (1925); see Nenius, Found: The Times, the Man, the Company 336 (1954). But see Bechau & Kahn, Integration in the Oil Industry 454 (1959).

10. Converse & Huey, Elements of Marketing 199 (3d ed. 1947) (savings on “salesmen, advertising, sales promotion, sales managers, buyers”). See also Girdner, supra note 7; Frank, supra note 9, at 179, 190-91. These expenses also include handling, transportation (geographical cross-hauling), and credit losses.

11. A familiar example of this is the “Swiss Army” knife, with saw, file, corkscrew, awl, bottle opener, screwdriver, can opener, and scissors, in one package. While this tool may be practical for the person who needs all of these items, the person needing only a few of them who had to buy it because nothing else was available would find himself paying for tools he did not need. Cf. Davis, Vertical Integration in the Textile Industries 2 (1938) (“Production policies of individual businesses are often attuned to speculative factors in intermediate markets and not related to the demand for finished
Stability advantages exist irrespective of the method of vertical integration chosen, i.e., contract or ownership. But the degree of realization of these and other benefits is dependent upon the particular form adopted. The two methods differ, for example, in the degree of control and flexibility offered; other relevant factors are labor costs and tax consequences.

**Control**

The chief distinction between ownership and contract as devices for vertical integration is the means of control available for coordination of the organizations involved. Ownership integration maximizes control—exerted by corporate directives and enforced by status sanctions. Control is necessarily more indirect when contract integration is employed. The traditional contract remedies—damages, rescission, perhaps specific performance—are the overt sanctions available. The threat of nonrenewal is, however, often equally potent. For many purposes, these indirect sanctions control the integrated firm as effectively as the status sanctions of ownership. But whenever con-

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1. See note 48 infra and accompanying text.
2. Under asset ownership, this method of control and enforcement is direct. Under stock ownership, control is exerted in two stages. The integrating firm votes the stock, and the directors thus elected issue the directives and apply the status sanctions, as well as being subject to them.
3. See note 48 infra and accompanying text.
4. The manufacturer does not have to possess resources to be able to command them; and, whatever the facts of ownership, the operations by which material and parts converge into cars represent a single technical process. It is control of design and sales which gives the manufacturer his strategic position; the importance of complete corporation integration is easily and frequently overemphasized.


Contract integration can be made more effective by establishing close relationships between integrating firms.

Successful subcontracting . . . regards the operations of the supplier as part of a continuous process, leading up to and including the operations in the buyer's own plant. In this concept, the supplier's material control, production efficiency, scheduling, and service, are definitely the concern of the buyer and his company, to be handled with the maximum of cooperation and mutual assistance. So far as the subcontracts are concerned, the supplier's operations are a part of his customer's operation, even though they are carried on under a different roof and a different management.

HEINRITZ, PURCHASING 314 (1947); see FOLTS, op. cit. supra note 7, at 172.

control is crucial to secure supply or adequate quality, business has found it advisable to supplement, and even to replace, contract by ownership integration.\textsuperscript{14} For example, backward vertical integration by ownership increased greatly in the period immediately following World War II, because many producers were never sure when and whether they would get another shipment of raw materials as a result of widespread material shortages and consequent private rationing.\textsuperscript{15}

**Flexibility**

The correlatives of control are responsibility and commitment. Because of its fixed investment, the enterprise vertically integrated through ownership

\textsuperscript{14} According to Davis, *Vertical Integration in the Textile Industries* 10-11 (1938), backward integration by contract in textile manufacture has been very successful, but forward integration by contract has not, and has ended up in full merger to assure adequate coordination and quality control. See also Frank, *supra* note 1, at 179, 185-86 (ownership integration is by far the best assurance of stability of operations).

Examples of supplementing contract integration with ownership may be found in the cases. See Atlantic Ref. Co. v. Hodgman, 13 F.2d 781, 782 (3d Cir. 1926); Goodyear Tire & Rubber Co., 22 F.T.C. 232, 271-72 (1936).


\textsuperscript{15} Another common risk-reducing purpose is protection against shortages of supply. During the early postwar years this motivation dominated, because supply shortages were absolute; many producers were never sure when and whether they would get another shipment. This danger of complete cut-off in raw material supply does not fit into economic doctrine, because theoretically it is always possible to get supplies by bidding up prices a little more. But theory overlooks the phenomenon of private rationing, where suppliers keep prices rigid for wide ranges of demand and dole out their product according to past purchases or some other non-price scheme.

Dean, *Capital Budgeting* 142-43 (1951).

In 1940 Safeway reported that meat purchasing involved "no procurement problems worth mentioning." Fortune, Oct. 1940, p. 132. But by 1945 Safeway was being forced, it claimed, to integrate because the big meat packers weren't allocating it its share of meat. The Interstate Merchant, May 6, 1945, p. 1. Before World War II, the fixed policy of Republic Steel Corporation was to be not committed for more than half of its ore requirements so that the company could take advantage of cheaper "distress" ore. But after the war, the company had to go "over to . . . ownership or long-term contract[s] . . . [to] become covered or integrated," because of the necessity of having a secure supply. *Hearings Before the Subcommittee on Study of Monopoly Power of the House Committee on the Judiciary*, 81st Cong., 2d Sess., ser. 14, pt. 4a, at 240 (1959) (testimony of C. M. White, President, Republic Steel).
may show considerable inertia and inflexibility. Contract integration, on the other hand, offers the parties a high degree of flexibility, facilitating adaptation to changing circumstances, and the prompt reallocation of productive facilities. This is of particular importance in industries which must respond quickly to design or style changes, or those characterized by rapid technological obsolescence, or changes in the business cycle.

Flexibility may conflict, however, with stability. In a very real sense, the two are antithetical. To the extent that an organization makes commitments

16. KIMBALL & KIMBALL, PRINCIPLES OF INDUSTRIAL ORGANIZATION 62 (6th ed. 1947). ("... organization is 'tuned up' to produce a given product, it is difficult, and expensive to change over to new models or different products.") Such inflexibility may particularly be present when the enterprise is very large. For a discussion of size as a factor leading to inflexibility, see text at note 26 infra.

17. Much of the inertia of the vertical concern arises from fixed investments that are not easily put to new uses or readily liquidated. The best way to attain the maximum degree of flexibility would be to restrict all investment to materials and to have all manufacturing operations carried on by contract operators. This in effect is the policy which nearly all retailers and wholesalers have followed in venturing into the textile business. It should be emphasized that integration through ownership of goods rather than through facilities depends on the availability of reliable and competent contract operations.

DAVIS, VERTICAL INTEGRATION IN THE TEXTILE INDUSTRIES 117-18 (1938); see id. at 8; Bus. Week, July 7, 1951, pp. 116, 118; id., June 30, 1951, p. 72; Baker, Peacetime Customers: Toolbuilding Subs, Steel, Nov. 19, 1951, p. 70. But see Aviation Week, Sept. 24, 1951, p. 155 (assertion that the translation of aircraft design changes into production is slower when production is subcontracted out).

18. If frequent changes in design are demanded, why not, as in days of old, shift some of the risk and expense to the manufacturer of parts? Instead of investing in a plant to make radiators, when today's style may be outdated tomorrow, it may be advisable from year to year selectively to buy from the radiator specialist the product which fits best with current designs. The invention of a better brake may render an ancillary brake plant obsolete; it may be better policy for the manufacturer to buy from an independent concern licensed to make it. Since the appeal of style is strong in respect to some parts and weak as regards others, a partial rather than a complete integration may be the answer to a serious problem.


However, risk can be so severe that it is impossible to integrate by contract and ownership integration is "thrust upon" a manufacturer. See 1955 SEN. HEARINGS pt. 8, at 4298-99 (GM claimed it purchased Euclid to demonstrate the utility of "hydramatic" to the construction equipment industry after the latter refused to believe it would work); DAVIS, op. cit. supra note 17, at 71-72; Klaw, Lever's Artful Dodging, Fortune, June 1959, p. 125, at 158 (when Monsanto developed a new, low-sudsing detergent, it was unable to interest the soap industry in the product, and was forced to integrate vertically into distribution; when "all" caught on, it was able to sell out to Lever, see note 354 infra and accompanying text). See also HALE & HALE, MARKET POWER: SIZE AND SHAPE UNDER THE SHERMAN ACT 237 n.13, 463-64 (1958). This may account for the use of vertical joint-venture agreements in the development of new product lines. See id. at 144 & n.20 (horizontal combinations).
to insure stability of operations, it must surrender a degree of flexibility. Ownership is generally the ultimate commitment, and by the same token it minimizes flexibility. Contract offers the parties their choice of the full range from complete commitment and no flexibility to complete flexibility and almost no commitment. Thus, contract ideally makes it possible for the parties to select whatever mixture of flexibility and stability they deem optimal. Of course, what is the optimum for one contracting party may not be optimum for the other. Hence, the extent to which each party approximates his optimum will depend on his bargaining position.

Bargaining power is a crucial consideration in contract integration. Normally, when risk is shifted, its assumption must be paid for. For example, when parts are subcontracted out and a risk is shifted, the prime contractor may have to pay a premium over the immediate cost he would incur if he chose to manufacture the parts himself. Thus, he still would carry the “cost” of the shifted risk. But the prime contractor may succeed in transferring to the weaker party the potential adverse effects of a change in the business cycle or some other such business variable. Thus, often a manufacturer has utilized contract integration to shift losses stemming from fluctuations in raw material and inventory values “to other corporate units who can levy no...

19. Bargaining power, it should be realized, need not be the result of monopoly power. It may result from the normal “stickiness” of a “workably” competitive market. See Adelman, supra note 1, at 48.


21. Some production men have expressed dislike for dealing with subcontractors because of the high profit subs exact. See Casting Off the Subcontractor, Bus. Week, Aug. 15, 1953, p. 43. However, this same source discusses the slump which hit subcontractors after the Korean truce. Parts subcontractors suffer great fluctuations in their business activity between boom and recession, because their customers buy at peak demand periods, rather than expand, but use their own plant facilities when business slackens. See also Make It or Buy It: Which Pays Off?, Bus. Week, July 3, 1954, p. 106; Squeeze on Subcontractors, Am. Machinist, Aug. 26, 1957, p. 144; Coughlin, Job Shops Hard Hit by Pullbacks, Aviation Week, Oct. 11, 1954, p. 21; Coughlin, Small Business Fights for Survival, id. Oct. 4, 1954, p. 16. It would appear then that the allegedly high prices subs charge reflect risks they face.


In the automobile industry, manufacturers appear usually to control the terms of contracts with suppliers. See 1955 Sen. Hearings pt. 7, 2982, 2999, 3001-02 (use of GM form contracts); id. pt. 6, at 2269 (“economic colonialism” alleged); id. at 2323 (allegation GM coerces its suppliers). Chrysler is said to have a policy of obtaining suppliers to whom it is the most important customer. United States v. E. I. du Pont de Nemours & Co., 353 U.S. 586, 634 (1957) (dissenting opinion). The size of automobile industry suppliers may give some clue to their bargaining power. Three-quarters of Chrysler and General Motors suppliers have less than 100 employees. ORGANIZATION FOR EUROPEAN ECONOMIC COOPERATION, SOME ASPECTS OF THE MOTOR VEHICLE INDUSTRY IN THE U.S.A. 26 (1953). In the aviation industry, half of the subcontractors on a typical Air Force contract have less than 25 employees, while about 70% have less than 50...
demand upon his treasury . . . [and] who go under quietly. . . .”

And the structure of the industry may be such that the unfavorable position of the weaker party will persist indefinitely.25

Economies and Diseconomies of Scale

The choice between production of or contracting for any component of the firm's product also depends in part on the optimum size of the production unit of the total product, including the component in question. When the size of the plant producing the component is comparatively small, combined ownership might increase efficiency and thus result in greater economies of scale. In such a situation, ownership integration would be practical. But when the production unit required for the component to be added is disproportionately large, consolidated ownership could decrease overall efficiency, and thus be economically unfeasible.

Large size may prove disadvantageous to an enterprise. A recent study suggests that increases in internal lines of communication in an organization decrease its rate of response to stimuli and render it less flexible with respect to change.26 This would seem to confirm the skeptical views some writers
have expressed regarding the relative efficiency of the large organization. Nor are inertia and stolidity the only diseconomies of scale. Decreased efficiency may result from spreading management "too thin" or spreading it among "hired hands" who lack entrepreneurial drive. And bigness can prove a curse to its possessor as well as to its alleged victims. Public and governmental hostility to the large concern is always a relevant consideration. Anti-chain-store legislation is an example of this hostility, as is resistance by some consumers against dealing with large corporations. Factors such as these favor integration by contract.

On the other hand, large size brings an organization greater bargaining power, greater access to financing, and sometimes greater political influence. Size may make feasible the hiring of more expensive personnel or the establishment of a management training program. And a large enterprise is more able to diversify, thus lessening the risk of loss due to changes in the business environment.

To secure the technological benefits of large-scale production, firms often


28. Ridgeway, Administration of Manufacturer-Dealer Systems, 1 Ad. Science Q. 464, 470 (1957); Cross, Vertical Integration in the Oil Industry, Harv. Bus. Rev., July-Aug. 1953, p. 69, at 77-78; Cole, supra note 1, at 27, 30-31. According to Slichter, maintaining administrative control over a large organization is often prevented by employees and department heads who "doctor" the records because they are "more interested in how efficient they appear to be than in how efficient they are; they often use more ingenuity in covering up their shortcomings than in improving their efficiency." Slichter, op. cit. supra note 26, at 137-38.

29. In recognition of political and public sentiment against big business, some oil companies decided not to use ownership vertical integration but to use contract vertical integration instead. McLean & Haigh, The Growth of Integrated Oil Companies 510 (1954); 1 Whitney, Antitrust Policies 125 (1958). See also Cole, supra note 1, at 36-37. Perhaps a similar motive was involved in GM's decision to buy refrigerator parts from American Motors "which it could as well make for itself." It has been alleged that this was done to "silence" American as a "protestant." 1955 Sen. Hearings pt. 6, at 2323.


33. Like conglomerate integration, although perhaps less effectively, vertical integration by ownership makes it possible for an enterprise to put its "eggs" in different baskets. See Boatwright, Vertical Integration in the Petroleum Industry, in Vertical Integration in Marketing 136, 138-39 (Bureau Econ. & Bus. Research, U. Ill., No. 74, 1952); McLean & Haigh, op. cit. supra note 29, at 83; Cross, supra note 28, at 77.
integrate by contract with a "specialist" who enjoys economies of scale in manufacture, purchasing, and research not attainable by the integrating firm.44 Even highly integrated industries, such as automobile manufacturing, have found it to their advantage not to manufacture all of their own parts.45 Certainly few industries care to make their own nuts and bolts or paper clips.

Moreover, reliance on the specialist releases capital for the firm to employ elsewhere in its operations or makes it possible for the firm to operate with a smaller capital investment. In effect, the firm is able to tap the capital resources of other firms in other industries. For infant industries, this may be of great importance,46 and the availability of such specialists decreases the capital barrier to entry.47

34. Where the technical unit requires to be large, not because all the processes require to be on a large scale, but because one process requires to be on a large scale, that process tends to be separated off and performed for the main industry by another subsidiary industry. Thus most motor firms buy ... parts ... . By such outside purchase the small firm can obtain almost all the economies available to the large firm. It is at a disadvantage only in so far as its smaller demands enable it to drive a less hard bargain with the specialist firm.


Moreover, in distribution, for example, forward integration by the manufacturer may be unsuccessful because the retail store requires many items, a "full line," to operate successfully; but the manufacturer cannot efficiently produce a full line. Thus the outlet must purchase from more than one manufacturer. Craig & Gabler, The Competitive Struggle for Market Control, 209 Annals 84, 91-92 (1940); McLean & Haigh, How Business Corporations Grow, Harv. Bus. Rev., Nov.-Dec. 1954, pp. 81, 87.

For an example of specialization in distribution to achieve sufficient output to make production economical, see Bus. Week, Oct. 9, 1954, p. 108 (Whirlpool Corp. got "on top of the home laundry market ... [through] the Kenmore line of washers, dryers, and ironers" which it sells Sears Roebuck, building volume to reduce the effect of overhead costs); cf. FTC, MANUFACTURE AND DISTRIBUTION OF FARM IMPLEMENTS 103 (1948) (specialty farm equipment manufacturers cannot afford ownership integration of distribution).

35. Thus, Arvin Industries supplied parts (e.g. mufflers, defroster parts, structural supports, interior trim) for 17 of the 19 passenger car makes in 1957. ARVIN INDUSTRIES, INC. ANN. REP., 1957, p. 7, 17.

The dominant characteristic of the independent parts fabricators as well as the allied parts divisions of the vehicle manufacturer is that they tend to specialize in relatively short lines of parts which have common manufacturing requirements and require a high degree of skill and efficiency. In fact the basic competitive strength of the parts fabricator as against the integrated vehicle manufacture is the cost advantage which the 'specialist' has in spreading the heavy yet inescapable outlay for research, tools and dies, over several contracts.


Occasionally, small ownership-integrated enterprises have shifted to contract integration because they could not keep up with technological progress requiring a higher and higher degree of specialization. See Against Make or Buy Tide, Bus. Week, March 19, 1955, p. 194.

36. See note 77 infra.

37. Capital barriers to entry are discussed in text at notes 74-76 infra.
Federal Taxation

In some limited circumstances, tax considerations are of importance in determining the form of integration to be adopted. Since a comprehensive treatment of the relevant sections of the Internal Revenue Code is beyond the scope of this Article, some provisions which may bear most directly on the problem will be pointed out. Ownership integration may have tax advantages. The shareholders of the acquired firm might avoid realizing income when the stock of the acquiring firm, rather than cash, is exchanged for the stock of the acquired firm.\(^{38}\) Or, in the case of a sale of a closely held corporation, they might be able to convert, on favorable terms, nonmarketable securities into marketable ones, in preparation for anticipated estate taxes.\(^{39}\) And when the stock is exchanged for money, the shareholders may be able to close out their investment at capital gains rates rather than continue in an enterprise yielding income taxable at ordinary rates and subject to continuing business risk.\(^{40}\) Further, it is possible at times to convert a loss carryover into money rather than to lose it through bankruptcy or expiration of the five-year period for carrying losses forward.\(^{41}\) For the acquiring corporation, the possibility of a forward carryover of past losses of the acquired firm may be significant. For example, when Willys and Kaiser merged, Kaiser had a sixty million dollar loss carryover which Willys could use to offset future taxable earnings.\(^{42}\) It should be realized that such factors are relevant only in rather special circumstances and generally play no role in a decision whether to integrate by contract or ownership.

Turning to the question of tax economies with the vertically integrated system already in operation, tax advantages of ownership are slight. One difference is the possibility of filing a consolidated return.\(^{43}\) This substantially decreases the likelihood that losses or loss carryovers at some level of production will not be dissipated by nonuse. However, the tax rate on consolidated returns is two per cent higher.\(^{44}\) And it is most doubtful that contract integrated production can continue in the face of losses at some levels and gains at others long enough for loss carryovers to accumulate and be lost.\(^{45}\) Renegotiation of the contract or failure of the losing firm are more probable.\(^{46}\) Finally, owner-

\(^{38}\) **Int. Rev. Code of 1954, § 354.**


\(^{40}\) **Int. Rev. Code of 1954, §§ 1201(b), 1221-23.**

\(^{41}\) **Int. Rev. Code of 1954, §§ 172, 381-82, 1212; see Western Pac. R.R. v. Western Pac. R.R., 345 U.S. 247, 276-77 (1953) (dissent) (tax loss is asset of corporation just like any other asset, and its seller is entitled to reasonable compensation).**


\(^{43}\) **Int. Rev. Code of 1954, § 1501.**

\(^{44}\) **Int. Rev. Code of 1954, § 1503(a).**

\(^{45}\) With respect to recoupment under ownership vertical integration see note 61 infra.

\(^{46}\) Another possibility is that the firm saddled with an onerous contract will buy up the other firm. Thus, in 1926 General Motors bought all of Fisher Body's stock to terminate an unfavorable long term requirements contract. *1955 Sen. Hearings* pt. 8, p. 4299.
ship integration offered an opportunity at various times in the past to reduce excess profits taxes by increasing the "invested capital" or historic income base. But, by and large, these tax possibilities do not significantly favor ownership integration over contract.

Labor Relations

Reliance on contract may, in some industries, enable an already unionized firm to add a product component without paying the higher labor costs which could attend expansion by ownership. The operation of the minimum wage and hour laws might be similarly avoided. These factors would apparently point to contract integration. But ownership integration may strengthen the bargaining power of the combined entity and thus perhaps result in lower total labor costs than would obtain if both firms bargain independently. Unified ownership might, on the other hand, force the integrated firm to bar-


50. Moreover, a contractor may suffer from the labor troubles of his suppliers. In 1953, shortly after Studebaker attained full production, a ten-week strike in the plant of one of its important suppliers forced it to reduce production sharply. Immediately after strike settlement and resumption of full production, the retail car market collapsed and Studebaker found that it had no opportunity to sell its cars. Studebaker Corp. Ann. Rep., 1953, p. 4-5; see Champion Motors Co. Ann. Rep., 1948 (sales dropped 46% partly due to supplier strike); N.Y. Times, April 1, 1959, p. 51, col. 5 (Chrysler losses from glass supplier's strike spur adoption of tapered ownership integration).
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gain as part of the integrating firm’s industry, where "follow the leader" wage trends upward may be more prevalent. If such was the case, labor would be ultimately cheaper under contract integration.

A Mixed System of Integration

The weight to be given the foregoing factors varies with the business cycle and long range trends of each industry. Their significance also changes as the firm passes through different stages in its history. Hence, business organizations tend to experiment with mixed systems—using contract for some factors of production or distribution and ownership for others. Moreover, for some components, enterprises blend the two devices, adopting a “tapered” system of integration. This scheme is frequently em-

51. "The greater the percentage of company manufacture of the products distributed by the company, the greater would be the effect of the swings of the business cycle [risk of idle plant, need to lay off]." Culliton, op. cit. supra note 25, at 72.

52. "Young companies, just as companies in young industries, are subject to many more risks than better established ones. Frequently their working capital is not plentiful. Any new company faces risks, many of which cannot be foreseen ... sufficient to make it worthwhile to avoid the additional risks involved in making things which can be bought." Culliton, op. cit. supra note 25, at 78. See also Seltzer, A Financial History of the American Automobile Industry 28-29, 48, 264-73 (1928).

53. Culliton, op. cit. supra note 25, at 78; 1955 Senate Hearings pt. 2, at 545 (ownership integration desirable only for auto makers producing more than 800 cars a day).

Firms frequently shift from ownership to contract to enjoy the benefits of new developments by independent suppliers. See, e.g., id. pt. 7, at 2997 (shift from ownership to contract for Buick torque converter, Chevrolet clutch plate). See also Clark & Clark, Principles of Marketing 145 (3d ed. 1942).

54. "Greater size may be an advantage in purchasing or in marketing but a disadvantage in manufacturing; or it may be an advantage in manufacturing but a disadvantage in marketing. Every enterprise, therefore, is a compromise between the advantages of largeness or smallness in some departments and the disadvantages in others." Slichter, Modern Economic Society 134 (1931).

The automobile industry is one of the best examples of an integrated industry using a mixed system. See Adams, supra note 13, at 58-59; Ford Motor Co., Forty Years 15 (1943) ("Self-integrated as it [Ford] is, it still looks to more than 6000 firms ... for parts and services"); 1955 Senate Hearings pt. 2, at 652; id. pt. 7, at 3638. The aviation industry is another good example, see Aviation Week, Nov. 22, 1954, p. 20 (52% of contract dollar goes to subs), as is electronic manufacturing, see Karpeck, supra note 22, at 82 (60% to subcontractors).

55. "Tapered integration" differs from a mixed integration in that the latter involves the use of contract for some factors of production or distribution and ownership for
ployed where it is difficult to keep outputs at successive stages in balance with one another.

**THE IMPACT ON THE ECONOMY**

An optimum blend of ownership integration, contract integration, and spot market purchasing probably makes the average firm most adaptable to changes in its business environment and provides for the best allocation of its resources. But the ideal allocation of resources from the firm's viewpoint may not prove consonant with the optimum allocation of goods and services in the economic or social system as a whole.

Vertical integration, whether by contract or ownership, necessarily forecloses access to a segment of the market, since competitors of the integrating firm often can no longer deal with the integrated enterprise. Because of such foreclosure, vertical integration has been viewed as an evil in itself. The wrongs others while the former involves the use of contract for securing part of the firm's needs for some factor and ownership for the rest of that same factor. The rationale of tapered integration is discussed in Adams, supra note 13, at 57-59. For an example of tapered integration, see 1955 Sen. Hearings pt. 7, at 3004-05 (Chevrolet procured 50% of its clutch plate requirements from Borg & Beck in 1954 but manufactured the other 50% itself).

56. See Dean, Managerial Economics 117 (1951); Folts, Introduction to Industrial Management 172 (1938); Davis, Vertical Integration in the Textile Industries 87 (1938) ("... [1]ntegrated companies today might profitably accept unbalanced operations as the normal way in which they have to do business and, wherever possible, adjust their organizations accordingly.")

The Richfield Oil Co. has had a striking history of unbalanced operations. United Oil Co., a crude oil producer purchased the Richfield Oil Co., then primarily a refiner and distributor, in 1923 "to secure an assured outlet for its production." The merged concern's subsequent "expansion in marketing and refining proved to be the company's undoing, for it could not purchase a sufficient supply of crude oil at reasonable cost." In 1931, the company went into receivership. When Richfield was reorganized, finally, in 1938, its integration was out of balance; refining capacity was six times its crude production and station outlets were few and poor. Richfield then entered exploration and also made long-term output contracts with producers in a major new oil field. This resulted in crude production exceeding refining capacity. Hence, a new round of station and refinery building began. Brief for Richfield Oil Co., United States v. Standard Oil Co., Trade Rep. (1959 Trade Cas.) § 69399 (S.D. Cal. June 19, 1959) (consent decree). Richfield eventually found itself a defendant in two antitrust cases brought by the Government, discussed in notes 166-74 infra and accompanying text.

Another reason for adopting tapered integration is that the contract procurement system and ownership procurement system can be compared or even played off against one another. The firm can use "its own processing costs as a standard by which to judge the fairness of prices quoted by outside suppliers," Culliton, op. cit. supra note 25, at 87 & n.3, or it can provide “competition in costs for [its] own departments,” by using the outsiders as the standard, Bethel, Essentials of Industrial Management 163 (1954); Make It or Buy It: Which Pays Off?, Bus. Week, July 3, 1954, p. 106 (“keep its own engineering and design people on their toes”). Moreover, the firm can use the outside supplier's "low prices as a bargaining tool to explain to the union why higher wages can't be absorbed." Ibid.

57. See United States v. Yellow Cab Co., 332 U.S. 218, 224-25, 226-27 (1947); cf. Anchor Serum Co. v. FTC, 217 F.2d 867 (7th Cir. 1954). Compare the Justice Depart-
envisioned by this point of view are injury either to competitors or to the integrated firm. Obviously, competitors of the integrating firm may "suffer" as a result of adoption of the contract or ownership integration system if an important outlet or supplier is foreclosed, or if the integrating firm can reduce costs and therefore reduce prices and expand its market share. Competitors may be forced into integration in order to expand if not to exist. And integrated firms "suffer" economically if subordinated to the interests of the integrating firm. Finally, firms which decline integration may lose business if a would-be integrator therefore refuses to deal with them. Should these injuries, in themselves, be redressed by the law, or should they be classified as *damnnum absque injuria*? This problem is a recurrent theme in part II of this study.

By contrast, vertical integration might be regarded contrary to public policy only when its result is the restriction of competition. If such a standard were adopted, it would be necessary to consider whether integration ever restricts competition, and if so, under what conditions. Despite its admitted adverse effect on competitors, critics of the injury-to-competitors approach have denied that vertical integration, as such, has detrimental effects on competition. On the contrary, they argue, vertical integration protects the public interest to the extent that it increases efficiency and makes possible by-passing of "toll gates" resulting from monopoly or imperfect competition. "To prevent firms from branching vertically . . . would amount to protecting existing monopolists in their position, and to serve notice on potential monopolists that the business risks of exploitive behavior were henceforth very much less." In the language of one writer, "it is always horizontal market power, and not integration into other levels, which is important." Such writers have exploded the charges that vertical concentration restrains competition by making recoupment from level to level possible, by allowing extra profits from level to level, or by facilitating price "squeezes." These studies have made an invaluable contribution position (wrongful in itself) with the Court view (not wrongful in itself) in United States v. Paramount Pictures, Inc., 334 U.S. 131, 173-74 (1948); United States v. Columbia Steel Co., 334 U.S. 495, 519, 523-26 (1948).

58. See notes 22-24 supra.


62. Recoupment is the notion that the integrated firm can subsidize unprofitable operations at one level by raising prices at another level. The "squeeze" is predatory price-cutting on one level supported by recoupment. The premise behind such fallacies that integration makes it possible to extract more than one layer of profit from the industry is that each integrated level can make its own profit. The premise, however, is false: There
bution to our knowledge of the economics of integration. Recent studies, particularly those of Professor Bain, have demonstrated, however, that competition can be impaired when vertical integration is utilized in conjunction with existing market imperfections to make new entry into the industry unprofitable and thus strengthen horizontal power. In particular, such barriers to competition can be raised by vertical integration when horizontal power in one market or stage of production creates "leverage" for the extension of the power to bar entry at another level. Thus, vertical integration plus horizontal power can impair competition to a greater extent than could the exercise of horizontal power alone.63

In part II, the case law on vertical integration is analyzed principally in terms of this "leverage" standard: does the integration arrangement impair competition more seriously than would horizontal power at each level of production if exerted independently? In the view of the authors, this is the criterion the Supreme Court attempts to apply in the cases. The remainder of part I is devoted to an analysis of the economic basis of this standard: the theory of barriers to entry.

Barriers to Entry

Entry to an industry will be barred when a prospective new competitor must anticipate lower net returns than the established firms enjoy. Given this condition, the structure of an industry will remain undisturbed.64 Manipulation of the industry's prices or costs is the means through which the prospective entrant's net returns can be kept down. Price manipulation is essentially a horizontal phenomenon, but cost manipulation has both horizontal and vertical aspects. The firm or firms seeking to bar entry must have sufficient market power over total output in the market (i.e., over price) or over the factors of production and distribution (i.e., over cost). This is to say that entry can be more easily barred in monopolistic or oligopolistic industries

is only one maximizing point for the industry, dependent only on the product's demand curve and its production costs. Thus, there is only one economic rent realizable in a vertical chain of production and distribution. Addition to the enterprise of levels vertically integrated by ownership will require further investment and entail additional risks—the profit earned, over and beyond the technological economies integration offers, will be a "normal" one, except in very special circumstances. See Bork, supra note 61, at 198-200; Adelman, supra note 60, at 41-43.


64. See BAIN 12-13. The same conclusions apply to expansion of or maintenance of existing competition in the industry. Compare id. at 5.
than in freely competitive industries; this proposition is almost tautological. 65  

A second condition for barring entry is that production on a very small scale be uneconomical; conversely, that only fairly large firms will be efficient. 66  

Given these two conditions, entry of new competition can be prevented when market price and output are maintained at such a level that the addition to the total market output (the "lump") contributed by an entrant of minimal efficient size will depress market prices below the costs of the prospective entrant. 67  

Hence, the wise monopolist will not price his goods at a level which exacts the full (short-run) toll of his power. Instead, he will exercise forbearance and maximize for the long run by setting his price just high enough over marginal costs as not to encourage entry. 68  

Whether such a monopolist should be prosecuted for his activities is outside the scope of this Article. 69  

No vertical integration problem here exists.  

The vertical integration problem arises when the monopolist attempts to bar entry by influencing the costs of the factors of production or distribution. For example, suppose a refiner could gain control of the world's ore deposits. He could thus bar entry into refining (of which he has no monopoly). Monopolization of the factors of production is not essential; control over but a part of the ore supply can drive its short-run price level high enough to increase the cost of production drastically. 70  

But one may ask why, in a rational business world, does the hypothetical monopolist not abandon his refining operations and concentrate his activities on ore in which his monopoly profits ("economic rent") are apparently earned. 71  

There are at least two explanations for persistence in vertical integration by our monopolist. First, there are the true economies of vertical integration, irrespective of economic rent considerations. Second, without the vertical relationship, the supply monopoly frequently may not yield its full benefit because a bilateral monopoly situation might develop: someone else might, in the terms of our hypothetical, attain a refining monopoly. If there are monopolies at two levels in separate hands, the countervailing power of each monopolist may force the other to share the monopoly "take." 72  

To
put it somewhat differently, horizontal power at either level may provide leverage over the other level. The mining monopolist in this situation would appear to need vertical integration into refining to assure profit maximization. In this case vertical integration is a means of protecting the advantages of horizontal power.

Barriers to entry can also be raised by forward integration which raises the distribution costs of potential competitors. Preemption of the choice outlets imposes on the prospective entrant the high cost of developing his own outlets—a fixed outlay—or else the choice of using inferior outlets which entail higher variable costs.

If we move from monopoly to oligopoly, the same considerations are relevant: collective, even though not collusive, integration can grant the oligopolists security against new entry and consequent disruption of market price and profit stability.

Still another way to increase costs for the prospective entrant is to raise the risk capital outlay necessary for his successful entry: if enough of the market can be foreclosed by vertical integration, newcomers will be forced to make rather than buy. They will have to enter, if at all, as ownership integrated enterprises. Thus they will be forced to wager a bigger stake, and this may discourage them from betting. Moreover, even if prospective entrants are not “discouraged,” they may find it far more difficult to raise, say

opponents. STIGLER, THEORY OF PRICE 240-41 (rev. ed. 1952); FELLNER, COMPETITION AMONG THE FEW 240-52 (1949); Spengler, Vertical Integration and Antitrust Policy, 58 J. POL. ECON. 347 (1950). However, a games theory solution is given in HOFFMAN, LARGE-SCALE ORGANIZATION IN THE FOOD INDUSTRIES, 161-65 (TNEC Monograph No. 35). Paradoxically, all solutions show that the public is worse off under bilateral monopoly than under a vertically integrated single monopoly. Price to the consumer is higher and output is lower. As Bork observes, this analysis has interesting results for countervailing power theories. Bork, supra note 61, at 196 n.128.

73. MILLER, UNFAIR COMPETITION 212 (1941); Lockhart & Sacks, The Relevance of Economic Factors in Determining Whether Exclusive Arrangements Violate Section 3 of the Clayton Act, 65 HARV. L. REV. 913, 922 (1952).

In Standard Fashion Co. v. Magrane-Houston Co., 258 U.S. 346 (1922), where ownership integration of department stores by pattern manufacturers was impractical, tying up those outlets by contract seems to have raised an absolute barricade against entry. Compare the situation in FTC v. Motion Picture Advertising Serv. Co., 344 U.S. 392 (1953), discussed in text at notes 226-38 infra, where ownership integration of theaters in order to secure their available screen time for advertisements would have been out of the question. Whenever ownership integration is impractical because of imbalance of the scale of operations at the two levels, see note 56 supra, and the number of outlets at the larger scale operation are limited, exclusive dealing contracts may successfully bar entry to the level with smaller scale of operation.

74. For a discussion of the oil industry in this context, see Rostow & Sachs, Entry Into the Oil Refining Business: Vertical Integration Re-Examined, 61 YALE L.J. 856, 911-14 (1952); Dirlam & Kahn, Leadership and Conflict in the Pricing of Gasoline, 61 YALE L.J. 818, 842-55 (1952); de CHAZEAU & KAHN, op. cit. supra note 61, ch. 5. But see Adelman, supra note 60, at 61-62.
fifty million dollars than ten million dollars.\textsuperscript{76} Of course this latter obstacle presupposes imperfection or discontinuity in the capital market.\textsuperscript{76}

Finally, an integration system may incidentally affect competition in other industries, or prevent the very existence of other industries. For example, had the machine parts industry been tied up by integration, the growth of the automobile industry might have been dangerously threatened. The infant industry would probably not have been able to afford the ownership-integrated parts-manufacturing facilities it now has.\textsuperscript{77}

\textsuperscript{75} But the larger firm may be willing to make a larger bet, and therefore conglomerate mergers may at times act to introduce new competition into areas of the economy where capital barriers to entry do exist. See \textit{Bain} 215. The tax laws may be significant in this connection. If a loss bankrupts a corporation, there will be no loss carry-over for future years and the owners will pay 100\% of the loss from their investment. But when a going enterprise suffers a loss, there is a 52\% income tax cushion. Of course, any gains are also cushioned this way, but the firm which takes a risk which may bankrupt it will pay a 52\% tax if it wins the bet and 100\% of the loss if it does not win. See \textit{Int. Rev. Code} or 1954, § 11; note 41 \textit{supra}.

Essentially, the problem is that of when to buy insurance and when to be a self-insurer and take a chance. It is not sufficient to compare “expectation” measured in cash, with the premium, measured in cash. The “expectation” must be corrected in terms of the overall consequences of a loss. For this reason doubling the stakes, even keeping the odds constant, can discourage wagerers. See Friedman & Savage, \textit{The Utility Analysis of Choices Involving Risk}, 56 J. Pol. Econ. 279, 285 n.16, 295 n.32 (1948). See also Huff, \textit{The Mathematics of Sex, Gambling, and Insurance}, Harper’s Magazine, Sept. 1959, pp. 69, 71-72.

The importance of this type of barrier will be decreased when the risk can be shared among several enterprises. Although no one of five firms, each with $10 million of assets, may be daring enough to take a $10 million “flyer,” the pool of the five might be willing. See note 18 \textit{supra}. Imperfection in the risk capital market, particularly with respect to information, probably makes for obstacles in forming such pools. Capital market imperfections are discussed generally in note 76 \textit{infra}.

Given a perfect capital market, the opportunity to invest $10 million at an “extraordinary” rate of return, tied in with an investment of another $50 million at an “ordinary” rate, would appear about as attractive as the opportunity to invest $10 million alone at the extraordinary rate. In either case, the total economic rent accrued is equal. See Bork, \textit{supra} note 61, at 195.

\textsuperscript{76} According to Bain, such barriers do exist in many industries. “It is suggested that large capital requirements place the potential entrant at a disadvantage, because he cannot secure the requisite funds at a rate as low as that available to established firms through the capital markets or through internal financing.” \textit{Bain} 215. The problems confronting small business in securing equity and loan capital are discussed in Cahn, \textit{Capital for Small Business: Sources and Methods}, 24 \textit{Law & Contemp. Probl.} 27 (1939) (collecting other literature). See also Comment, 47 \textit{Calif. L. Rev.} 144, 144-45 (1959) (collecting authorities); Adelman, \textit{Integration and Antitrust Policy}, 63 \textit{Harv. L. Rev.} 27, 33-34 (1949); \textit{De Chazeau & Kahn}, \textit{op. cit. supra} note 61, at 273-75 (discussing access to capital in the petroleum industry).

\textsuperscript{77} The wide distribution of the capital burdens of automobile manufacture involved a considerable diffusion of the risks of the industry, and therefore greatly diminished their deterrent influence. Speculative as the industry appeared, potential producers did not face the necessity of risking large sums of capital in their operations:
Thus, when component producers are "free," new enterprises can operate on a shoestring through contract integration, and not be forced to assume the heavy capital burden of full ownership integration before beginning. Existence of such intermediate open markets may be necessary for innovation and technological progress to occur. Probably, this problem is more serious when the factors of production or distribution are integrated by ownership rather than more directly by the immediate manufacture of the product was shared by numerous independent enterprises which supplied the capital required for the manufacturing operations as such, and which assumed the immediate subsidiary risks involved therein. On the other hand, responsibility for the final product, and the essential risks of final design, integration of the purchased components, and factory sales, did not face those who actually, though indirectly, provided the bulk of the capital employed. Resources that would not be directly committed to the fortunes of automobile production proper were nevertheless attracted to and then supplied by hundreds of enterprises engaged in providing materials, components, and sales facilities for the new product. Mobility in the employment of capital did not in this case require a wholesale assumption of new risks, nor, on the surface, a radical diversion of existing capital. In other words, there was a far greater divorce between the functions of responsibility-taking and capital contribution than is commonly thought possible in new and speculative industries. In consequence, the diversion of capital to the automobile industry was greatly facilitated.


78. A new product may command capital resources not only by diverting these from other goods, but also by effecting the utilization of hitherto idle utilities residing in existing capital equipment. Such increases in the efficiency of capital are tantamount to absolute additions to the stock of capital; and while they are rarely reflected in pecuniary measurements, they may be of great practical importance, particularly in a period of improving technology. Some of the capital early devoted to automobile production came from the idle resources of machine shops and similar establishments, which added automobile components to their lines of products without, at first, diminishing their output of other goods or increasing their capital equipment.

Speaking broadly, we may say that a wide distribution of capital among industries supplying raw materials, subproducts, and various kinds of services, and an improving technology, facilitate the mobility of capital. The concentration of capital in highly integrated industries, on the other hand, would seem to render capital less mobile. If, twenty-five or thirty years ago, industrial practice had required that each final product be produced by a highly integrated enterprise that directly controlled the sources of the raw materials and all the intermediate manufacturing stages, entrance into the automobile industry necessarily would have entailed a considerable measure of concentrated risk. Indirect diversion of capital, with its attendant diffusion of risks, would have been virtually impossible. In contrast with what has actually taken place, the development of automobile manufacture...
than contract, because of the more permanent and effective market isolation that the former causes.

II. THE IMPACT OF THE ANTITRUST LAWS ON VERTICAL INTEGRATION

In our legal system, the antitrust laws provide the framework within which any conflict between the public and private interest in vertical integration is to be resolved. The antitrust laws relevant to vertical integration are sections 1 and 2 of the Sherman Act,79 sections 380 and 781 of the Clayton Act, and section 5 of the Federal Trade Commission Act.82 Section 1 forbids the unreasonable restraint of trade by contract, combination, or conspiracy. Section 2 condemns monopolization of trade. Section 3 proscribes sales made on condition that the buyer not deal in the goods of the seller's competitors, whenever the effect may be to lessen competition substantially. Section 7 forbids acquisitions when the effect may be substantially to lessen competition. Section 5 interdicts monopolization of trade. These statutes reflect different and somewhat inconsistent legislative purposes, and as a result internal tensions exist within the total antitrust structure,83 and within the individual statutes.84 Perhaps the most serious of the tensions is generated by the competition-competitors dichotomy. According to the injury-to-competition standard, the antitrust laws are directed to restraints which affect or are intended to affect the market itself—affect it in

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79. 26 Stat. 209, (1890) as amended, 15 U.S.C. §§ 1-2 (1958). (The relevant text of this and other pertinent cited statutes is given in Appendix to this Article.)


83. "I am not unaware that the policies directed at maintaining effective competition, as expressed in the Sherman Law, the Clayton Act, as amended by the Robinson-Patman Act, and the Federal Trade Commission Act, are difficult to formulate and not altogether harmonious." FTC v. Motion Picture Advertising Serv. Co., 344 U.S. 392, 405 (1953). (Frankfurter, J., dissenting). "It is also incumbent upon us to seek to rationalize the four statutes directed toward a common end and make of them, to the extent that what Congress has written permits, a harmonious body of law." Id. at 405. See also United States v. United Shoe Mach. Corp., 110 F. Supp. 295, 342 (D. Mass. 1953) (no single pattern).

84. "The legislative solution is often to write two opposing ideas into a statute . . . . A hiatus may be left in a law . . . . The necessity to fill in the gap is then presented to the court. And the judges are left at large in a field that the legislature lacked capacity to define." Address by Mr. Justice Douglas Before Section of Judicial Administration of American Bar Association, Seattle, Sept. 8, 1948, quoted in Fleisching, Ten Thousand Commandments: A Story of the Antitrust Laws 2 (1951).
the form of higher prices, poorer quality, or decreased supply. In this view, restraints without significant market effect are not prohibited. According to the injury-to-competitors approach, the antitrust laws exist also to prevent injury to those trading in the market place, irrespective of other competitive effects. Under this standard, antitrust performs a tort law function. As we shall see, the ideals of protection of competition and protection of competitors are often irreconcilable. And it is as yet unclear which view will prevail.

Additional tension exists between the "per se" and "rule of reason" approaches to antitrust violations. A rule-of-reason standard requires the courts to assay the economic consequences of business behavior and to ban only behavior which is "unreasonable" in purpose or effect. But the application of this standard necessitates a comprehensive and costly economic analysis, a task which may be "most ill-suited for courts." Therefore, a catalogue of "per se" offenses has emerged. Within this area, the courts are relieved of the necessity of a comprehensive economic analysis; these offenses are banned because they belong to a forbidden category whose purpose and effect are declared to be necessarily anticompetitive. Nevertheless, the problem facing the court in these cases has not become one of "mere characterization." The per se categories are still being enlarged and modified. And within the domain of the rule of reason further tensions have developed. A power test vies with a performance test. Should possession of power to restrain competition be sufficient for a violation of the Sherman Act, or must that power be exercised with anticompetitive effect? Moreover, "having a substantial effect" and

85. See Apex Hosiery Co. v. Leader, 310 U.S. 469, 493, 500 (1940). Such effects include also prevention of innovation which might lower prices or improve quality.

... [T]he object of the antitrust laws is to achieve what may be called a "workably" or "effectively" competitive organization of industry and commerce, and not "pure" or "perfect" competition. Correspondingly, ... the idea of workable or effective competition is the main component of the rule of reason in defining offenses under Sections 1 and 2 of the Sherman Act.

The judicial norm is now close to what the economists have classified as workable competition.

Rostow & Sachs, Entry Into the Oil Refining Business, 61 Yale L.J. 856, 860-61 (1952). The various definitions of workable competition, according to the authors, "turn on the same crucial elements—the capacity of buyers to take advantage of rivalry among sellers, the inability of sellers to exercise appreciable control over the price at which they sell, and the absence of cost or other barriers to the entry of new firms." Id. at 61. See also ATT'Y GEN. NAT'L COMM. ANTITRUST REP. ch. 7 (1955).

For a brief but penetrating discussion of the competition-competitors dichotomy, see Adelman, Book Review, 46 Am. Econ. Rev. 481 (1956).


87. Performance testing is a method which has often been recommended by those who think there is as much danger from too much competition as from too little. It has become a slogan for those who fear the dangers of straight-jacketing industry by any unequivocal prohibitions or uniform general rules, and who specifically dislike any concepts calling for per se or presumptively illegal market status
"justified by good business reasons" have competed with one another as tests of the reasonableness of market practices. Some of these tensions appear quiescent at the present moment. Still, we can expect new tensions to appear in the future, for antitrust seems to be a particularly dialectical branch of the law—the life of antitrust is strife.

All of the disharmonies of antitrust are echoed in the case law of vertical integration, and as a result the cases show considerable vacillation. Because different statutes apply to different forms of vertical integration, uncertainty as to the appropriate standard to be used in each case has been further increased. The early integration cases, which announce the major themes, have received thorough treatment elsewhere and need not be discussed in detail here. For our purposes, it is sufficient to begin with Standard Oil Co. v. United States [Standard Stations], in which the contours of current ver-

or behavior. Some like to call this the rule of reason approach. In an extreme form this would call for reviewing the effects of everything—even price-fixing agreements. Performance tests seek conclusions as to whether, for example, profits are too high, whether innovation is rapid enough, whether production is in the right size firms, whether there is an efficient adjustment of capacity to output, whether there is a proper avoidance of waste in selling activities, whether new firms have entered or can enter the industry readily, whether or not the restrictive agreements themselves contain the seeds of their own destruction, whether or not equality of bargaining power is achieved with either or both suppliers or customers, and as many more criteria as any bright analyst can invent. All of these sum up to a general evaluation of performance to tell whether the public is being adequately served.

These performance criteria may raise more problems than they solve. Economists are no better than lawyers at measuring with uncalibrated rulers.


88. At present, the former test governs, despite the presence of "good business reasons." Thus, when the efficiencies of integration come into conflict with the dictates of competition, the law is that the latter must prevail.

If, indeed, this [anticompetitive effect] were a result of the [integration] system, it would seem unimportant that a short-run by-product of stability may have been greater efficiency and lower costs, for it is the theory of the antitrust laws that the long-run advantage of the community depends upon the removal of restraints upon competition. See Fashion Originators' Guild v. Federal Trade Comm'n, 312 U.S. 457, 467-68; United States v. Aluminum Co. of America, 148 F.2d 416, 427-29 (C. A. 2d Cir.).


89. See the articles by Adelman, supra note 60, and Bork, supra note 61.

90. 337 U.S. 293 (1949).
tical integration law emerge, and in which the Supreme Court attempted to harmonize the conflicting policy goals of the antitrust laws by a doctrinal synthesis. *Standard Stations*, together with *FTC v. Motion Picture Advertising Serv. Co.* [MPAS] and *United States v. E. I. du Pont de Nemours & Co.* [du Pont-GM], reveals the pattern of the current law of vertical integration. *Standard Stations* applied a market foreclosure test to forward vertical integration by requirements contracts, an arrangement explicitly covered by section 3 of the Clayton Act. *MPAS* applied this test to backward integration by contract, a situation not covered by section 3 but within the scope of section 1 of the Sherman Act. *Du Pont-GM*, decided under section 7 of the Clayton Act, carried the same test over to a vertical integration system based on stock ownership.

Despite the movement by the Supreme Court toward a single antitrust standard for vertical integration arrangements, the law in the area has not been completely synthesized. In a series of court of appeals decisions, differences in the wording of the various statutes have been emphasized and legal distinctions established between antitrust private damages actions and public prosecutions. As a result, there has been new legislation in this area and pressure for more. Part II begins with an analysis of the major governmental intervention cases. A discussion of the case law on private antitrust suits follows. Part II concludes with an examination of actual and possible changes in the antitrust laws.

**Government Action Against Integration**

*The Rule of Standard Stations: Section 3 and Quantitative Substantiality*

*Standard Stations* is the richest and the most difficult of all the vertical integration cases. Each of the tensions that has been mentioned within the structure of antitrust is revealed in the *Standard Stations* decision. As the leading case on integration by contract, it has been the subject of extensive commentary and controversy. The decision may raise as many problems as it settles, but the rule of *Standard Stations* is one which must be reckoned with in all vertical integration cases, and comprehension of this rule is essential to evaluation of the impact of antitrust upon integration.

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91. 344 U.S. 392 (1953).
93. See notes 361-468 infra and accompanying text. The Court has not yet spoken on this question, declining to grant certiorari and review the opinions.
94. See notes 469-514 infra and accompanying text.
Standard Stations involved the distribution of petroleum products and automobile accessories. The oil industry is characterized by oligopolist producers who are integrated with their retail outlets by requirements contracts. These contracts bound the outlets to obtain all of the products they sold from the integrating producer. Defendant's contracts covered sixteen per cent of all the retail gasoline outlets in the West, 6.7 per cent of the gasoline sold in the West, and about fifty-eight million dollars in annual sales. Standard's sales through company-owned outlets and to industrial users brought its total share of the Western gasoline market up to twenty-three per cent, while its six leading competitors, who employed similar exclusive dealing arrangements, absorbed, according to the Court, another forty-two per cent of the market. The seven majors controlled seventy-six per cent of all stations in the West.

The Justice Department brought suit under section 1 of the Sherman Act and section 3 of the Clayton Act to enjoin Standard from entering into or enforcing these exclusive contracts. The district court found for the Government on both counts. The Supreme Court affirmed, basing its decision solely on section 3. Mr. Justice Frankfurter's opinion for the majority was accompanied by dissenting opinions from Mr. Justice Jackson and Mr. Justice Douglas.

Mr. Justice Douglas opposed condemnation of Standard's contracts because this would, in his view, drive Standard into vertical integration by agency or by outright ownership of the stations, a situation which, at that time, was subject to a much more lenient antitrust standard than contract integration. The net result would be to turn entrepreneurs into clerks, causing dilution of "local leadership" and a "serious loss in citizenship" to the "village." Essentially,

96. 337 U.S. at 295.
97. *Ibid.* This 42% is an extremely conservative figure, since it excludes the industrial sales by Standard's six leading competitors. The record is silent on the latter. United States Brief, p. 10 n.5. Thus the percentage of total gallonage sold by the Big Seven must have exceeded 65%.

In addition to its gasoline requirements contracts, Standard maintained a policy of requiring many dealers to carry only TBA (tires, batteries, accessories) furnished by Standard. 337 U.S. at 296-97. The Supreme Court opinion does not emphasize the TBA tie-in, *id.* at 305 n.8, aspect of the case.

Even though the problems presented by exclusive dealing and by tying contracts are clearly related, tying arrangements are not included in this Article. Different treatment has been accorded by the courts to the two devices. See, e.g., Frankfurter, *J.*, in *Standard Stations*, discussing the differing policy considerations, *id.* at 305-08; TBA provisions as tie-ins, *id.* at 305 n.8. A treatment of tie-ins would have to include patent usage problems. See generally Bowman, *Tying Arrangements and the Leverage Problem, 67 Yale L.J.* 19 (1957); Lockhart & Sacks, *supra* note 95, at 942-54; Turner, *The Validity of Tying Arrangements Under the Antitrust Laws, 72 Harv. L. Rev.* 50 (1958).
the Douglas dissent is based on prospective injury to the integrated dealers which will have social repercussions; this is akin to an "injury to competitors" argument.

The Jackson dissent, in which two other Justices joined, is based on contrary arguments. Jackson viewed the market as an already imperfect one in which the oligopolists battle it out, using the dealers as pawns, "the instrumentalities through which competition . . . is waged."\textsuperscript{103} Exclusive dealing, according to his view, is an offsetting market imperfection\textsuperscript{104} which increases rather than decreases competition. Hence, Jackson opposed the banning of Standard's contract integration, because the system did not result in injury to competition.

While these opposing dissents both tend to a conclusion of legality, the

\textsuperscript{103} Id. at 323.

\textsuperscript{104} But see Dirlam & Kahn, \textit{Antitrust Law and the Big Buyer: Another Look at the A & P Case}, 60 J. Pol. Econ. 118 (1952) ("[W]here given markets are in some respects incorrigibly imperfect, an attempt to enforce more perfect competition in other respects may produce a poorer rather than a superior economic performance. Workable competition in inevitably imperfect situations, may require offsetting imperfections . . . . [But] the requirements of workable competition do not offer a blanket indorsement of all offsetting imperfections . . . .")
Frankfurter opinion for the majority ingeniously arrived at a contrary result by synthesizing the “injury to competition” and “injury to competitors” standards. The opinion began by examining the role of the rule of reason in a section 3 case, questioning whether it is necessary to show actual or probable anticompetitive effects of the exclusive dealing arrangements or whether it is enough simply to show that “a substantial portion of commerce is affected.”

The court mentioned four tests which would be appropriate, were the former standard adopted: whether “competition has flourished despite use of the contracts,” “the conformity of the length of their term to the reasonable requirements of [business],” “the status of the defendant as a struggling newcomer or an established competitor,” and “perhaps most important . . . defendant’s degree of market control.” These tests were rejected on three grounds. First, their use would run counter to legislative mandate. The investigation required “would . . . stultify the force of Congress’ declaration that requirements contracts are to be prohibited whenever their effect ‘may be’ to substantially lessen competition.” Second, “serious difficulties [of economic analysis] would attend the attempt to apply these tests,” and the task would prove one “most ill-suited for . . . courts.” Finally, the tests are inconclusive, since lack of anticompetitive effect is no proof that, but for the integration system, competition in the industry would not have been even keener. Thus, a rule of reason approach based on elaborate economic analysis was rejected. In place of an actual “performance” test, the majority advanced what is essentially a “power” test. Section 3 is violated when “a substantial portion of commerce is affected,” that is, when “competition has been foreclosed in a substantial share of the line of commerce.” Since “observance by a dealer of his requirements contract with Standard does effectively foreclose whatever opportunity there might be for competing suppliers to attract his patronage, . . . [and] in view of the widespread adoption of such contracts by Standard’s competitors . . . Standard’s use of the contracts creates just such a potential clog on competition as it was the purpose of § 3 to remove.”

105. 337 U.S. at 299.
106. Id. at 308. Of these tests, the first and fourth are substantial effect tests, while the second and third are “good business reasons” tests.
107. It is submitted that rejection of these tests by the Court indicates only that it regards them as possibly sufficient although not necessary.
108. 337 U.S. at 313. But see Lockhart & Sacks, supra note 95, at 936-37.
109. 337 U.S. at 308, 310.
110. Id. at 309-10. For a discussion of the economic consequences of an alternative system of distribution, see de CHAZEAU & KAHN, op. cit. supra note 61, at 517-19.
111. 337 U.S. at 299, 314.
112. Id. at 314.
The majority crossed the formidable bridge from injury to competitors to injury to competition by analyzing the meaning of the word "may" in section 3.

When it is remembered that all the other major suppliers have also been using requirements contracts, and when it is noted that the relative share of the business which fell to each has remained about the same during the period of their use, it would not be farfetched to infer that their effect has been to enable the established suppliers individually to maintain their own standing and at the same time collectively, even though not collusively, to prevent a late arrival from wresting away more than an insignificant portion of the market.\(^{1}\)

The rule of *Standard Stations* is, then: when competitors are foreclosed from a substantial enough share of the market, it is not farfetched to infer substantial lessening of competition.\(^{114}\) This is the so-called rule of quantitative substantiality.\(^{115}\)

To Mr. Justice Jackson, the majority interpretation of "may" in section 3 was unjustifiable. "It is indispensable to the Government's case to establish that either the actual or the probable effect of the accused arrangement is to substantially lessen competition or tend to create monopoly."\(^{116}\) He denied that foreclosure of a substantial share of the market can "automatically bring the accused arrangement within the prohibitions of the statute."\(^{117}\) "May" does not justify the movement from injury to competitors to injury to competition.

The number of dealers and the volume of sales covered by the arrangement of course was sufficient to be substantial. That is to say, this arrangement operated on enough commerce to violate the Act, provided its effects were substantially to lessen competition or tend to create a monopoly. But proof of their quantity does not prove that they had this forbidden quality; and the assumption that they did, without proof, seems to me unwarranted.\(^{118}\)

Thus, in Jackson's view, it is farfetched to move from injury to competitors to injury to competition upon a mere showing of foreclosure of a share,

\(^{113}\) *Id.* at 309.

\(^{114}\) For a discussion of the multiple meanings of the word "substantial" in antitrust law, see text at notes 129-34 infra.

\(^{115}\) See 337 U.S. at 298. Citations to the sizeable literature on quantitative substantiality are collected in *Handler, Antitrust in Perspective* 136-37, 143 (1957). See, particularly, *Att'y Gen. Nat'l Comm. Antitrust Rep.* 122 & n.26, 142 n.51, 149 (1955). See also *Hearings Before the Antitrust Subcommittee, supra* note 106, at 1966 ("Now we have the Chairman of the FTC trying to graft onto that bill a lot of economic hocus-pocus which does not belong there"); *id.* at 2360-64, 2442-2528 (FTC chairman examined and criticized for not following *Standard Stations* rule in *Maico Co.* as Medina, J., did in *Dictograph*); *id.* at 2244 (Handler-Celler colloquy).

\(^{116}\) 337 U.S. at 321.

\(^{117}\) *Id.* at 322.

\(^{118}\) *Ibid.*

\(^{119}\) The Jackson interpretation does not do full justice to the majority opinion to the extent that it criticizes it for moving from injury to competitors to injury to com-
no matter how substantial, of the market to competitors.\textsuperscript{120} Moreover, it is not enough for the inference of injury not to be "farfetched." The injury must be actual or, at least, probable.

The rule of Standard Stations was also criticized in the Jackson dissent as a per se rule because it looks only to market shares rather than to actual market effect: "I cannot agree that the requirements contract is \textit{per se} an illegal one under the antitrust law, and that is the substance of what the Court seems to hold."\textsuperscript{121} Perhaps this characterization is extreme. The standard announced is not a per se rule in the sense of the rule for price fixing under \textit{United States v. Socony-Vacuum Oil Co.};\textsuperscript{122} it does not declare all requirements contracts illegal. On the other hand, the majority opinion made it clear that the Clayton Act standard does not require proof of actual anticompetitive effect.\textsuperscript{123}

The crucial problem in applying the rule of Standard Stations is the determination of how much of the market must be affected before foreclosure is "substantial." Critics of the case have interpreted the decision as enjoining Standard only because its requirements contracts foreclosed 6.7 per cent of the relevant market.\textsuperscript{124} Under their interpretation, any share of the market going at all beyond \textit{de minimis} meets the test of Standard Stations. There is some language in the decision supporting this view: among the tests the Court rejects for determining the "restrictive effect of requirements contracts" is "perhaps most important . . . the defendant's degree of market control."\textsuperscript{125} This passage may be read to mean that the court felt that any degree of market control which is "not insignificant" falls under the ban of section 3.\textsuperscript{126}
It is submitted, however, that the Court's intention was only to reject market domination by the individual defendant as a necessary prerequisite for a section 3 violation.\(^{127}\) The repeated emphasis on parallel use of exclusive contracts by the major oil companies and on the aggregate sixty-five per cent of the market foreclosed by similar distribution arrangements shows that the Court did not rely on 6.7 per cent as the share of the market satisfying the quantitative substantiality test. It was the "collective, even though not collusive," foreclosure of the market by the majors,\(^{128}\) rather than the individual foreclosure by Standard, which offended the Clayton Act.

To repeat the rule of *Standard Stations*: when competitors are foreclosed by integration contracts from a substantial enough share of the market, it is not farfetched to infer a substantial lessening of competition.\(^{120}\) The use of the word "substantial" in this formula requires careful analysis, however, for it has two distinct meanings in antitrust. The first sense of "substantial" is in distinction to the *de minimis of de minimis non curat lex*: insubstantial restraints of competition are ignored by the antitrust laws,\(^{130}\) but substantial restraints are proscribed. In this sense, "substantial" is the only alternative to "*de minimis*." To reduce confusion "substantial," in this Clayton Act sense, will henceforth be termed "significant." But the second sense of "substantial" is quite different. Whether a firm or group of firms forecloses a "substantial" share of the market is not determined by whether the share goes somewhat beyond *de minimis*. In this context, the substantiality continuum does not have only two sectors—substantial and insubstantial (*de minimis*); rather, there are three sectors—substantial, insubstantial (*de minimis*), and a large gray zone between them.

When the share of the market affected by integration is *de minimis*, it is farfetched to infer any significant (non-*de-minimis*) adverse effect on competition. Therefore the integrating firm would be innocent of an antitrust violation. When the share affected is substantial (large), it is not farfetched to infer a significant adverse effect on competition. Hence the defendant

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127. The Court declares that the prior case law "regarded domination of the market as *sufficient* in itself to support the inference that competition had been or probably would be lessened." 337 U.S. at 301. (Emphasis added.)

Minimally, the Court extends the prior case law position, that individual "domination of the market [*sufficient in itself to support the inference that competition*] may be substantially lessened, to the position that collective domination is also *sufficient to support that inference*. However, while collective dominance may be sufficient, is it necessary in the absence of individual domination? The "incipiency" doctrine, see note 270 *infra*, and the word "may" may perhaps carry the Court far further.

128. See text at note 113 *supra*. See also 337 U.S. at 314 ("widespread adoption").

129. See text at note 114 *supra*.

130. See, *e.g.*, United States v. Columbia Steel Co., 334 U.S. 495 (1948) (merger § 1); Apex Hosiery Co. v. Leader, 310 U.S. 469, 500 (1940) (conspiracy § 1); Klor's, Inc. v. Broadway-Hale Stores, 255 F.2d 214, 235 (9th Cir. 1958), *rev'd on other grounds*, 359 U.S. 207 (1959) (same); Fargo Glass & Paint Co. v. Globe Am. Corp., 201 F.2d 534 (7th Cir.), *cert. denied*, 345 U.S. 942 (1953) (§ 7). See also Northern Pac. Ry. v. United States, 356 U.S. 1, 6-7 (1958) (per se, § 1) (dictum); 337 U.S. at 312 & n.15.
would be guilty. And when the share affected is neither substantial nor de minimis, the integrating firm is entitled to the Scottish criminal law verdict of "not proved."

The border between the gray zone and the "black" zone of substantiality is wavering, blurred, and ill-defined. However, it would do injustice to Standard Stations to say that it abolishes the gray zone and assimilates it into the black zone. Even the word "may" does not carry the Court this far. "May" adds to the black zone of actual anticompetitive effect only a somewhat lighter black of potential anticompetitive effect. Unless integration, by substantially affecting the market, has at least a demonstrable potentiality (not necessarily probability) of significant anticompetitive effect, the rule of Standard Stations should not come into play.3

Restating the rule with more precision, then: when integration forecloses a substantial portion of the market, it is legitimate to infer a significant effect on competition, and, therefore, a violation of section 3.

Failure to distinguish between the two meanings of "substantial" has contributed to much confusion about quantitative substantiality. Use of "substantial" in two senses, without explicit differentiation, conceals the importance of the Court's move from quantity (degree to which the market is affected) to quality (effect upon overall competition). At the same time the justification for jumping the gap from quantity to quality rests in the proposition that the degree of vertical integration in the industry may have enabled "the established suppliers . . . to maintain their own standing and at the same time . . . prevent a late arrival from wresting away more than an insignificant portion of the market." This proposition views the potential anticompetitive effect of vertical integration as a barrier to entry problem. Is it really not far-fetched to infer existence of a barrier against entry into gasoline refining from the proportion of the retail market affected by integration?

Several different entry barriers may have existed in this industry. In its complaint, the Government alleged that Standard had tied up a substantial portion of the choice outlets. If it were proved that Standard, or Standard and the other six major refiners, had foreclosed independents or newcomers from the bulk of choice outlets, it might go far toward suggesting that a barrier

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131. Compare the "incipient incipiency" of § 5, note 276 infra.


133. See 337 U.S. at 298, 314.

134. See text at note 113 supra. "Since Standard's major competitors also distributed their gasoline under requirements contracts, it is possible that the cumulative foreclosure of retail outlets by the seven leading oil companies might have denied the small producers effective access to the consumer." Handler, op. cit. supra note 115, at 121 n.35.

135. Record, p. 6. See also id. at 4 ("positions of substantial impregnability against competitive invasion of their . . . areas"); 337 U.S. at 304 n.6.
rier to new competition had been erected.\textsuperscript{136} If outsiders were compelled to market through inferior outlets, they would be forced to incur higher distribution costs than the established Big Seven, thus limiting their ability to compete.\textsuperscript{137} This barrier to new competition would prove even more severe if the one-year requirements contracts were in reality perpetual contracts due to the high cost to dealers of switching suppliers.\textsuperscript{138}

However, the Government did not prove its allegation that Standard had preempted the choice outlets by means of its contracts. No evidence was even offered by the Government to prove the charge.\textsuperscript{139} Indeed, the record contains some evidence pointing to the conclusion that Standard's contracts covered, on the average, sub-standard stations. For example, in the Los Angeles area, Standard had contracts with 3.68 per cent of the outlets and sold only 2.43 per cent of retail gallonage through them.\textsuperscript{140} Thus, these stations sold only two-thirds as much gasoline as the average station.\textsuperscript{141} In the San Francisco area, Standard had 6.98 per cent of the stations in the area and sold 5.52 per cent of total area gallonage through them.\textsuperscript{142} This represents a twenty-one per cent below average showing.\textsuperscript{143} Los Angeles and San Fran-

\textsuperscript{136} Such a finding might also narrow the relevant market under consideration to favorably situated stations, where defendant's market percentages would be greater. By the same token, greater power over price in the relevant market might be apparent.

\textsuperscript{137} Unit distribution cost is inversely proportional to station gallonage. Brief for Appellants, p. 18; Record, p. 1862A.

\textsuperscript{138} See \textsc{Handler}, \textit{op. cit. supra} note 115 at 120-21; United States v. Richfield Oil Corp., 99 F. Supp. 280 (S.D. Cal. 1951) \textit{aff'd per curiam}, 343 U.S. 922 (1952), discussed in text accompanying notes 164-72 \textit{infra}; United States v. Sun Oil Co., \textsc{Trade Reg. Rep.} (1959 Trade Cas.) \textsection 69398, at 75506-07 (E.D. Pa. July 1, 1959) ("The changing over from one brand of petroleum products to another by a dealer subjects him to an economic hardship and even to the risk of a business failure."); \textsc{Hearings Before the Subcommittee on Antitrust and Monopoly Problems of the House Committee on the Judiciary, 84th Cong., 1st Sess. ser. 3, pt. 3, at 1930 (1955) (statement of E. V. Rostow) ("as a practical matter dealers would find it costly to change suppliers . . . in fact these arrangements were of indefinite, and extended duration"). \textit{But see} United States v. Standard Oil Co. 1958 \textsc{Trade Cas.} 74758, 74762 (S.D. Cal. Oct. 31, 1958) ("dealers would change from one defendant to another").

\textsuperscript{139} See Brief for Appellants, p. 12 n.13. As a result, the district court judge said to Government counsel, "[Y]ou have offered no testimony at all connected with geography, as well as to good corners or bad corners or anything else." Record, p. 1082. See \textit{id.} at 1023 ("nothing from which to argue that they got the choice station or did not").

\textsuperscript{140} Brief for Appellants, p. 29; Record, p. 1649.

\textsuperscript{141} The computation is 2.43\% ÷ 3.68\% = 67\%, and it compares the average Standard dealer station's gallonage with the average of all stations' gallonage.

\textsuperscript{142} Brief for Appellants, p. 29; Record, p. 1652.

\textsuperscript{143} The stations owned by Standard, however, made 85\% and 75\% above par showings in the Los Angeles and San Francisco areas. The average of Standard's six leading competitors was 2\% above and 1\% below par for the two areas. The independent refiners made 8\% and 16\% below par showing in these areas. See Record, pp. 1649, 1652.

The superior performances of Standard's owned stations may stem in part from preemption of favorable locations and the existence of municipal ordinances preventing the building of new stations. See Brief for Appellants, p. 12; Record, pp. 1081-82. \textit{But cf.}
cisco, however, are the most competitive areas in the Western market, the homes of frequent price wars,\textsuperscript{144} and it may be unsafe to generalize on the basis of statistics from those locales. In any event, we lack the information to decide whether a barrier to new competition was erected by imposition of higher unit distribution costs on newcomers.\textsuperscript{145}

Another possible barrier to entry might have resulted from Standard's policy of refusing to sell any gasoline to a dealer who also buys from another refiner.\textsuperscript{146} Had the other major refiners pursued the same policy, every dealer would have had to choose between either buying \textit{all} of his gasoline from the independents, or else buying \textit{none} from them. There could be no tapered system.\textsuperscript{147} Since being deprived of gasoline may quickly bankrupt dealers,\textsuperscript{148} it would seem understandable that they would prefer to deal with established majors than with newcomers who might not be able to provide them with a

Gasoline Retailer, June 3, 1959, p. 21, col. 1 (Standard's owned stations "did little better than break even" in 1958, according to its president.)

In general, Standard's owned stations made a better showing than Standard's contract stations. The owned stations, 3\% of the stations in the area, sold 6.8\% of taxable gallonage. The contract stations, 16\% of Western stations, sold 6.7\%. 337 U.S. at 295; Brief for Appellee, p. 7.

\textsuperscript{144} See \textit{Hearings Before Subcommittee No. 5 of the House Committee on Small Business}, 84th Cong., 1st Sess. 260-307 (1955); Gasoline Retailer, Dec. 3, 1958, p. 1, col. 5.

"The pervasive and continuing lack of balance [despite vertical integration] between the almost continually expanding operations of the major oil companies is the most important force that often impels them willy nilly into price competition or its equivalent." \textit{DE CHAZEAU & KAHN, INTEGRATION AND COMPETITION IN THE OIL INDUSTRY} 454 (1959). For a discussion of price wars and their causes, see Dirlam & Kahn, \textit{Leadership and Conflict in the Pricing of Gasoline}, 61 \textit{YALE L.J.} 818, 833-34 (1952); Rostow & Sachs, \textit{Entry Into the Oil Refining Business: Vertical Integration Re-Examined}, 61 \textit{YALE L.J.} 856, 866-67 (1952).

\textsuperscript{145} BAIN 279-81 suggests that entrants have higher unit sales promotion costs because of existing product differentiation barriers. But consideration of such problems is outside the scope of this study.

On the role of the independent under a system of vertical integration, see Adelman, supra note 103; Rostow & Sachs, supra note 144, at 863-70; \textit{DE CHAZEAU & KAHN, op. cit. supra} note 144, at 454-61, 519-52.

\textsuperscript{146} See Brief for Appellant, p. 15. \textit{Compare} Record, p. 1127 with id. at 241-42.

\textsuperscript{147} That the majors followed such a parallel policy was asserted in the Government's subsequent complaint against the major Western refiners. Amended Complaint, 1956, p. 37, United States v. Standard Oil Co., \textit{TRADE REG. REP.} (1959 Trade Cas.) \# 69399 (S.D. Cal. June 13, 1959) (consent decree). The claim was that the majors blacklisted any dealer who violated the understanding or contract that he deal exclusively with his supplier. Compare Fashion Originators' Guild of America v. FTC, 312 U.S. 457 (1941). The alleged result is that gasoline prices are stabilized at a higher level because dealers are prevented from having recourse to price-cutting independents. Amended complaint, supra at 42. \textit{But see} the consent decree in the case, United States v. Standard Oil Co., supra at 75533-34. ("It is understood that each consenting defendant is now supplying many dealers on a spot basis . . . "). discussed in note 167 infra.

\textsuperscript{148} See Brief of Union Oil Co., p. 20, United States v. Standard Oil Co., supra note 147.

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steady supply of gasoline. A newcomer might overcome this reluctance by entering the industry at a sufficiently large scale as to assure his being able to meet his dealers' full needs. This, however, would increase the capital requirements for entry. If, in the alternative, the major refiners did not follow a policy of refusing to deal with stations outside their integration system, entry on a smaller scale would be feasible since independent dealers could obtain supplementary gasoline supplies from the majors. Thus, adoption by the major competitors of an "all or nothing" policy with dealers may have raised a barrier to the entry of new competition into the industry. But, again, we lack sufficient information on which to base a judgment. In any case, what the Court condemned explicitly was a policy of requiring exclusive dealing from retailers, rather than a policy of refusal to deal with outsiders. Of course, the two are intimately related, but the Court's focus on the consummated contracts suggests that its decision did not rely on the consequences of the policy of refusing to deal.

149. See Lockhart & Sacks, The Relevance of Economic Factors in Determining Whether Exclusive Arrangements Violate Section 3 of the Clayton Act, 65 Harv. L. Rev. 913, 925 (1952). For an example of an active attempt to "discourage" dealers from handling new lines, see Belone Hearing Aid Co., 52 F.T.C. 830 (1956).

150. Query: Could a struggling newcomer afford to do this without himself exacting exclusive dealing contracts? See Excelsior Motor Mfg. & Supply Co. v. Sound Equip., Inc., 73 F.2d 725, 728 (7th Cir. 1934); B. S. Pearsall Butter Co. v. FTC, 292 Fed. 720 (7th Cir. 1923); Harley-Davidson Motor Co., 50 F.T.C. 1047, 1066 (1954).

151. The majors also have supply continuity problems. They meet them by swapping gasoline with one another when one is short in his supply. Record, pp. 272-73. If a newcomer could swap with the majors it would probably eliminate this problem. But the majors do not exchange with outsiders, according to some complaints. 1 Whitney, Antitrust Policies 172 (1958); Complaint, pp. 4, 20, 39, 40, 47, United States v. Standard Oil Co., Trade Reg. Rep. (1959 Trade Cas.) ¶ 69399 (S.D. Cal. June 13, 1959). But see Richfield Brief, p. 20, Appendix (deliveries to nondefendants). The consent decree in the foregoing case enjoins these conspiratorial refusals to exchange with nonmajors. Trade Reg. Rep. (1959 Trade Cas.) at 75529.

152. Such information would include at least sufficient qualitative or quantitative data on the refining side of the industry as to raise the likelihood of an incipient restraint of competition ("may" of § 3).

153. A case in which a court did consider the refusal to deal aspect of this problem is Mogul S.S. Co. v. McGregor, Gow, & Co., [1892] A.C. 25 (1891). A horizontal combination of shippers had agreed not to deal with shippers who used tramp steamers (or, according to other evidence, to charge a higher rate to such shippers). The "tramps" were ships which did not follow a regular schedule and which cut prices. Id. at 53-54. Since shippers could not depend on tramps for all their shipping needs, they could not afford to forego use of the organized lines belonging to the combination. As a result, the tramps were foreclosed from a considerable part of the market. In effect, the combination forced its rivals to establish a complete, year-around service as a condition of securing access to the market. Since the tramps could not—or would not—do this they were prevented from competing with the combination. However, the House of Lords held that the combination was a permissible means to extend trade and increase profit. The tramps were held to have no cause of action in conspiracy, although the horizontal agreement was unenforceable between the parties. Compare the dual rate shipping con-
Another possible barrier to competition may have resulted because economies of scale were unavailable to newcomers since too few retail outlets were accessible to them. This is probably what the Court meant when it stated that "requirements contracts . . . enable the established suppliers . . . collectively, even though not collusively, to prevent a late arrival from wresting away more than an insignificant portion of the market."

The record indicates that twenty-four per cent of the retail outlets in the West were not integrated with one of the seven major refiners. As to these outlets, we have no information about how many of them were, in a practical sense, available to a newcomer. If only so few of them were available as to prevent operation at an efficient scale, then entry was barred. But again on this point we have no data.

Thus, of the three possible barriers to entry which may have existed in the industry, none was established by the evidence the Government relied upon. On the basis of the data we are not entitled to conclude that any particular one of the three barriers existed. But may we consider that there is a possibility—of low order probability—that each existed? And are we then entitled to aggregate these separate low order probabilities into a higher order probability that some barrier existed? One might be tempted to answer affirmatively, because "courts are ill-suited" to indulge in comprehensive economic analysis.

Nevertheless, it would require no "economic extravaganza" for a court to put into the record sufficient data to justify a conclusion that barriers to entry may exist. In Standard Stations, there would have been little difficulty in introducing such evidence, assuming that it existed. Thus, as to choice locations, gallonage figures were available from state tax authorities. As to the stability of gasoline supplies obtainable from independents, testimony from such independent refiners with respect to regularity of their output and any consequent marketing problems they face could have been obtained. And as to economies of scale, testimony by expert witnesses regarding minimal efficient refiner size could have been secured. Because of the relative ease of securing some such economic data, the authors are in sympathy with Mr. Justice Jackson's position that the case should have been remanded to the District Court for further evidence. But the authors do not agree with the Jackson view that quantity of commerce affected cannot, by itself, justify the
inference of effect on competition. They in no way criticize the principles of quantitative substantiality and collective foreclosure invoked by the majority of the Court.

The Standard Stations opinion does not tell us, in terms of exact percentages of output or of dollar sales volumes, what share of the market is "substantial" in a requirements contracts case. It does not reveal whether the maximum lawful share in an individual foreclosure case would be larger or smaller than that in a collective foreclosure case. It is further uncertain whether the Court will adopt a flexible yardstick, varying with the market structure of individual industries. In Standard Stations, the Court was in the position of a man who knows he has about two hundred dollars in the bank, more or less, and who wants to write a check; this man has no problem if he writes a fifty dollar check, but if he writes a hundred eighty dollar check, he may overdraw his account. Whether the Supreme Court made an overdraft in its Standard Stations decision is by no means clear. But in

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159. "But proof of their quantity does not prove that they had this forbidden quality; and the assumption that they did, without proof, seems to me unwarranted." 337 U.S. at 322 (dissenting opinion of Jackson, J.); see note 120 supra.


161. Such reintroduction of a rule of reason into § 3 appears problematical at the present moment, but past antitrust experience suggests that this is by no means unlikely. See United States v. Columbia Steel Co., 334 U.S. 495, 528 (1948) ("The relative effect of percentage command of a market varies with the setting in which that factor is placed."). Under the standard of quantitative substantiality, evidence of lack of actual anticompetitive effect of a questioned integration practice is said to be inadmissible. See Dictograph Prods., Inc. v. FTC, 217 F.2d 821, 824 (2d Cir. 1954). When a substantial enough fraction of an industry is so affected by integration that it is not farfetched to infer a significant effect on competition in that industry, the antitrust laws ban the integration arrangements. However, economic evidence is relevant in determining how substantial a fraction must be affected in order to presume the forbidden effect. But whatever scope economic analysis is permitted in defining "substantiality," it can hardly be excluded in determining the relevant market. Much of the economic evidence the rule of Standard Stations is thought to exclude as irrelevant can be introduced as bearing on the definition of the relevant market. Thus, cross-elasticity of supply or demand can be used, in effect, to show lack of anticompetitive effect by demonstrating the need for a broader market definition. See United States v. E. I. du Pont de Nemours & Co., 351 U.S. 377 (1956) (cross-elasticity of demand); Times-Picayune Publishing Co. v. United States, 345 U.S. 594 (1952) (cross-elasticity of demand); United States v. Columbia Steel Co., 334 U.S. 495 (1948) (cross-elasticity of supply). The economist is not yet excluded from this "not insubstantial" field. See Adelman, Corporate Integration, in How To Comply With the Antitrust Laws 290, 304 (Van Cise & Dunn ed. 1954).

162. See Adelman, Integration and Antitrust Policy, 63 Harv. L. Rev. 27, 31 (1949).
subsequent cases, courts and the FTC appear to have drawn three hundred dollar checks along with fifty dollar checks.

**Avoiding Standard Stations: Agency, Understandings, Refusal to Deal.**

The impact of *Standard Stations* depends primarily on the extent to which it affects distribution systems, the availability of alternative devices, and the degree of control which can be exercised with their help.$^{103}$

With regard to gasoline marketing, Mr. Justice Douglas, as has been pointed out, criticized the majority for forcing the majors into either adopting ownership integration$^{164}$ or making use of the agency device, thus turning their retailers into clerks. The majority opinion seems to leave the way open for other alternative devices. In addition to mentioning fixed-quantity contracts,$^{163}$

163. According to the prosecuting attorney in *Standard Stations* and United States v. Richfield Oil Corp., 99 F. Supp. 280 (S.D. Cal. 1951), aff'd per curiam, 343 U.S. 922 (1952), the impact of the two decisions on the distribution patterns used by West Coast petroleum industries was negligible. Nondefendant members of the Big Seven, according to this testimony, did not attempt to comply with, or even evade, the decision; instead they ignored it, and "adopted a policy of a calculated business risk." *Hearings before Subcommittee No. 5 of the House Select Committee on Small Business*, 84th Cong., 1st Sess. 300-01 (1955). See also 1 WHITNEY, ANTITRUST POLICIES 131 (1958). *But see id.* at 130.

Given the institutional framework of gasoline marketing the effectiveness of banning exclusive arrangements has been questioned. "It contradicts both common sense and marketing experience to assume that the broad picture of single brand distribution would be appreciably altered even if dealers were completely free to choose." DE CHAZEAU & KAHN, *op. cit. supra* note 144, at 515-19. But the authors seem to concede that in the absence of exclusive arrangements "coercion" through integration might become less of a problem and access to the market might become easier for the independent. For the impact of *Standard Stations* on provisions or practices forcing the dealer to handle only company approved motor oil and TBA, see 1 WHITNEY, *op. cit. supra* at 129-33 ("in bringing the Standard Stations suit, the Department of Justice probably had in mind diminution of exclusive dealing in motor oil and TBA as much as or more than in gasoline").

164. See text at note 101 supra. See Rostow, *Over-All Size*, in *How To Comply With the Antitrust Laws* 311, 324 (Van Cise & Dunn ed. 1954), for the view that amendment of § 7 has swept away this alternative and therefore the basis for the dissent. Major refiners have decreased the number of owned outlets from 125,000 to 3,000 because of disadvantages of ownership integration. Presently, service stations fall into five categories, and number in each roughly as follows: (1) stations owned by the company—over 3,000; (2) "commission-type" stations—about 8,000; (3) stations leased from the supplier—90,000; (4) stations leased from a third party—15-20,000; and (5) stations owned by the dealer—60,000. 1 WHITNEY, *op. cit. supra* note 163, at 125-26. "[B]ut even today about 90 percent of all pumps and a somewhat smaller percentage of tanks are said to be owned by suppliers." 1 id. at 109. For a discussion of the use of consignment contracts in gasoline distribution, see *National Petroleum News*, July 1956, p. 93; DE CHAZEAU & KAHN, *op. cit. supra* note 144, at 426. Courts, as Richfield indicates, in interpreting the status of the "consignee" will continue to look to substance rather than form.

The legal consequences of ownership integration are discussed in this section of the Article in the text following note 289.
it may not have disturbed the validity of equipment contracts conditioned on
the understanding that “the right or license” of the dealer is dependent on
his using the equipment (tanks and pumps bearing the brand insignia of
the supplier) only for dispensing the products of the supplier. Finally,
consideration must be given to informal understandings of exclusive dealing
backed up by the sanction of refusal to deal.

Standard of California, in reaction to the opinion, did not turn its dealers
into employees. But it informed its equipment lessees that it still had the right
to control the use of its equipment to assure that it was used exclusively for

165. 337 U.S. at 303, 310.

The validity of such arrangements was tested and upheld in FTC v. Sinclair Ref. Co.,
261 U.S. 463 (1923). The Commission had prohibited these equipment contracts as un-
reasonable restraints on competition and unfair trade practices, since their practical effect
was directed in larger measure against dealers who did not have more than one pump.
The Supreme Court disagreed. It stressed that the contract did not contain a
covenant . . . which obligates the lessee not to sell the goods of another; and its
language cannot be so construed . . . . He may carry on business as his judgment
dictates and his means permit, save only that he cannot use the lessor’s equipment
for dispensing another’s brand. By investing a comparatively small sum, he can
buy an outfit and use it without hindrance. He can have respondent’s gasoline, with
the pump or without the pump, and many competitors seek to supply his needs.

Id. at 474. The validity of these equipment contracts, as the Court reasoned, could not be
challenged as unfair methods of competition:

The devices are not expensive—$300 to $500—can be purchased readily of makers
and, while convenient, they are not essential. The contract, open and fair upon its
face, provides an unconstrained recipient with free receptacle and pump for storing,
dispensing, advertising and protecting the lessor’s brand. The stuff is highly
inflammable and the method of handling it is important to the refiner. He is also
vitally interested in putting his brand within easy reach of consumers with ample
assurance of its genuineness. No purpose or power to acquire unlawful monopoly
has been disclosed, and the record does not show that the probable effect of the practice
will be unduly to lessen competition. Upon the contrary, it appears to have pro-
moted the public convenience by inducing many small dealers to enter the business
and put gasoline on sale at the crossroads.

Id. at 475. Mr. Justice Frankfurter, in distinguishing the Sinclair case, had this to say:
"The present case [Standard Stations] differs of course in the fact that a dealer who
has entered a requirements contract with Standard cannot consistently with that contract
sell the petroleum products of a competitor of Standard no matter how many pumps he
has . . . ." 337 U.S. at 303-04. Query: What effect, if any, has Northern Pac. Ry. v.
United States, 356 U.S. 1 (1958), on Sinclair? Since the basis for the decision in Sinclair
was, in part at least, that an exclusivity clause was aimed at the protection of the supplier’s
good will, is not the decision weakened by International Bus. Mach. Corp. v. United States,
298 U.S. 131 (1936)? One cannot overlook, however, the fact that IBM is the dominant
firm in its industry, as Sinclair was not.

Since the validity of this scheme presupposes, as Justice Frankfurter clearly indicates,
absence of an anticompetitive effect, see 337 U.S. at 303-04 n.6, the question may well be asked
whether the force of the decision does not depend on the opportunity of a dealer to sell
more than one brand (split-pumping). For a discussion of split-pumping, see de CHAZEAU
& KAHN, op. cit. supra note 144, at 516.
its products. Later on, we are also informed, it changed the status of some of its employees into consignees.165a

The alternatives of turning station lessees into agents, of using fixed-quantity contracts, and of using informal understandings of exclusivity backed up by the refusal-to-deal (cancellation) sanction were tested in United States v. Richfield Oil Corp.,166 which casts serious doubt on the availability of any of these devices as means of evading section 3. In that case, the Justice Department continued its attack on the West Coast oil oligopoly.167 Again the

165a. 1 Whitney, op. cit. supra note 163, at 127-28; De Chazeau & Kahn, op. cit. supra note 144, at 516.


The distribution system used by the west coast oil industry is now in large measure covered by the Final Judgment which has brought to an end nine years of litigation in which the Government attempted to strengthen its victory in Standard Stations and Richfield by breaking up the vertical integration systems used by the individual oil companies. The consent decree represents only a partial victory for the Government. Divestiture was not granted. Section XII A requires and directs each consenting defendant

(i) to offer to each dealer operating at any location in the Pacific States Area where he is being supplied with gasoline by such defendant . . . and

(ii) to grant to each such dealer who accepts such offer a supply agreement wherein such defendant undertakes to supply such dealer with gasoline for sale at such location. Each such agreement shall be for a term of at least three years; . . . and provided, further, that each such agreement with a dealer who, with the consent of such defendant, as a dealer occupies premises owned or leased by such defendant, shall contain a provision granting to such dealer a right to terminate said agreement upon ninety days' written notice.

Id. at 75531. (Emphasis added.)

The supply obligation need not exceed half of the dealer's requirements. Subsection XII(D), id. at 75532. Subsection G adds significantly: "It is understood that each consenting defendant is now supplying many dealers on a spot basis, or under supply contracts having less than a three-year term, with whom such defendant may be unwilling to enter into a supply agreement or a lease having a three-year term." Id. at 75532-33.

Subsection XIV enjoins the consenting defendants other than Standard Oil and Richfield from entering or enforcing any agreement with any dealer reseller in the Pacific states area, or forcing any such dealer to enter into any agreement, whereby such dealer agrees

(i) to purchase from said defendant or from a source designated by said defendant all or substantially all of such dealer's requirements of any refined petroleum product or of tires, batteries or accessories, or

(ii) to refrain from handling refined petroleum products or tires, batteries or accessories obtained from any other person;

Id. at 75533. Consignees are not resellers by virtue of a provision in definitional Section II (n).

Id. at 75528.

Standard Oil and Richfield are not affected by the exclusivity provision since they are covered by the original decrees. Section XIV, id. at 75533. The Texas Company is not a party to the consent decree. Id. at 75525.

Whatever may be the impact of the consent decree on the oil distribution system on
focus was on a contract integration system. In one set of contracts, covering stations which Richfield owned and leased to retailers ("leased-out" stations), an attempt was made by the defendant to bring the exclusive arrangements outside the scope of sections 1 and 3 by labelling them employment or agency contracts. This strategy was apparently based on *FTC v. Curtis Publishing Co.*, 168 and *United States v. General Elec. Co.* 169 In the former, agency was held to put a contract vertical integration system beyond the reach of section 3; in the latter, agency legitimized a price-fixing scheme which would otherwise have violated section 1. But in two earlier cases dealing with similar situations, the Supreme Court had not honored the agency defense because it found that no genuine agency relationship existed. 170 And in the recent case of *United States v. Masonite Corp.*, 171 the Court had declared that the agency label does not prevent a price-fixing scheme from running afoul of section 1. Thus, the *Richfield* district court had two techniques for disposal of the agency defense. It used both. It found as a fact that the dealers were independent businessmen, and it read *Masonite* to rule the agency defense out both under section 1 and section 3. 172

Another group of Richfield's contracts were for fixed amounts covering about eighty per cent of the dealer's requirements. However, there was an informal understanding that the dealer would buy one hundred per cent of his requirements from Richfield or Richfield would stop dealing with him. In some contracts there was the added sanction of being required, if cancelled, to repay Richfield for having painted the station with its colors and insignia. The court treated the combination of written and oral agreements as full requirements contracts despite their not being explicitly so denominated. 173

The West Coast, the force of the rules of law laid down in *Standard Stations* and *Richfield* is still intact as far as vertical integration in other industries is concerned.

169. 272 U.S. 476 (1926).
171. 316 U.S. 265 (1942).
172. For a criticism of the district court's finding that Richfield's service station lessees were independent business men, see de Chazeau & Kahn, op. cit. supra note 144, at 516.

A few months later the Fifth Circuit used *Curtis* to reverse an FTC cease and desist order against exclusive dealings contracts. Motion Picture Advertising Serv. Co. v. FTC, 194 F.2d 633 (5th Cir. 1952). On appeal, the Supreme Court reversed, 344 U.S. 392 (1953), on the ground, *inter alia*, that the proceedings were under § 1 rather than § 3, thereby making *Curtis* inapplicable. The Court then extended the *Masonite* § 1 rule for horizontal integration by contract to the § 1 vertical integration by contract context. *Id.* at 397. Although *Curtis* was distinguished rather than overruled directly, it would appear that there is little life left in it. For a discussion of agency as a device of forward integration, see Rifkind, *Division of Territories*, in How To Comply With the Antitrust Laws 127, 138 (Van Cise & Dunn ed. 1954).

173. Suppose each Richfield station sold about 10,000 gallons a month: Could Richfield, each year, make a "spot market" sale of 100,000 gallons to the station, informally
Accordingly, these contracts were held to be within the scope of sections 1 and 3.\textsuperscript{174}

\textit{Richfield} presented fairly simple problems of proof so far as the existence of exclusive dealing was concerned. The same was true of \textit{Standard Stations}. There was little doubt in either case that the supplier demanded and got exclusivity. In other cases, however, proof of exclusive dealing has been more difficult. The Justice Department failed in its suit for an injunction against J. I. Case Co., a farm equipment manufacturer.\textsuperscript{175} The Government alleged that exclusive dealing was an unwritten term of Case's franchise contracts and that Case forced its dealers to drop competing lines on pain of cancellation. Finding that the acts proved by the prosecution did not show any "pattern or policy on the part of Case to obtain an agreement or understanding from its dealers that they will not handle competing lines,"\textsuperscript{176} the court explained that cancellation of a dealer who carried dual lines might be coincidental or merely in pursuance of a sound business policy of dealer selection. In addition, the court found the fact that many dealers handled Case exclusively not to constitute evidence of an understanding forced upon them, because such practice was frequently a matter of volition.\textsuperscript{177} Finally, the court drew atten-

agrees that the dealer need not accept delivery of all his 100,000 gallons at once? It would hardly appear that such a "spot" sale would fare any better than the term contract for a fixed amount, which was followed in \textit{Richfield}.


The aftermath of the \textit{Richfield} decision was that the company cancelled all existing lease contracts and adopted a new leasing system under which rent was raised from 1\textcent{} to 2.5\textcent{} per gallon of gasoline sold. At the same time, Richfield dropped its tankwagon price, presumably below the level of the other majors' prices. As a result, it became cheaper for a dealer renting a Richfield-owned station to carry Richfield than the gasoline of another major—unless the competitor would meet Richfield's price. The Justice Department has indicated dissatisfaction with this practice. \textsc{I} \textsc{W} \textsc{H} \textsc{N} \textsc{T} \textsc{E} \textsc{Y}, \textsc{A} \textsc{N} \textsc{T} \textsc{I} \textsc{T} \textsc{R} \textsc{U} \textsc{S} \textsc{T} \textsc{P} \textsc{L} \textsc{I} \textsc{C} \textsc{E} \textsc{s} 120 (1957). Perhaps this scheme is not as objectionable as it appears. Richfield may be separating revenue from two components of its operations—the business of gasoline marketing and the business of being a landlord of gasoline stations. Maximization of revenue from each business would not appear unlawful unless horizontal monopolization at each level could be shown. \textit{Query:} Under the rule of Northern Pac. Ry. v. United States, 356 U.S. 1 (1958), would the new Richfield plan be a tie-in, illegal per se?

\textsuperscript{175} United States v. J. I. Case Co., 101 F. Supp. 856 (D. Minn. 1951). The suit was brought under § 1 and § 3.

\textsuperscript{176} Id. at 865.

\textsuperscript{177} \textit{Ibid.} \textit{V} \textit{o} \textit{l} \textit{e} \textit{n} \textit{t} \textit{i} \textit{n} \textit{u} \textit{j} \textit{i} \textit{r} \textit{i} \textit{a} is by no means an antitrust maxim. The prevailing view expressed in cases involving \textit{express} contracts for exclusive dealing is that acquiescence to the system by the dealers is no bar to Government prosecution. See FTC v. Motion Picture Advertising Serv. Co., 344 U.S. 392, 395-96 (1953); Anchor Serum Co. v. FTC, 217 F.2d 867, 870 (7th Cir. 1954); text at note 372 infra. Even in private damages actions the \textit{pari delicto} defense has been much eroded. See Red Rock Bottlers, Inc. v. Red Rock Cola Co., 1952-1953 Trade Cas. 67962 (N.D. Ga. 1952) (distributor

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tion to the fact that many Case dealers did in fact carry lines of other manufacturers, and that Case was subject to vigorous competition from other farm equipment manufacturers.

Reliance by a manufacturer on unwritten contract clauses backed up by the sanction of refusal to deal puts the prosecution at a severe disadvantage. As United States v. J. I. Case Co. reveals, the evidentiary problems may prove insuperable. When the prosecution has convincing evidence that exclusive dealing was in fact required however, there is no doctrinal problem. Thus, the FTC found a prima facie section 3 case made out against a manufacturer when evidence was introduced that he refused to deal with jobbers who dealt in the goods of his competitors. Although refusals to deal are not actionable as such under section 3, which requires a “sale,” the Commission aggregated the refusals to deal into a concerted plan from which it could be inferred that those sales which were consummated were made on the understanding that the buyer would stop dealing in the goods of the seller’s competitors.

The FTC and the Rule of Standard Stations: Quantitative Substantiality v. Injury to Competitors. Since Standard Stations the FTC has carried only two of its section 3 cases to the courts, Dictograph Prods., Inc. v. FTC, and Anchor Serum Co. v. FTC. These cases reveal a distinct evolution in the Commission’s application of the rule of Standard Stations. Dictograph was another Standard Stations: the respondent, “one of the industry’s three leaders, all or some of whom use this restrictive device,” had tied up over

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178. 101 F. Supp. at 866-67. Contrast United States v. General Motors Corp., 121 F.2d 376 (7th Cir.), cert. denied, 314 U.S. 618 (1941), where defendant GM attempted to show that many of its dealers did not finance through GMAC, the GM subsidiary with whom dealers allegedly had been coerced to deal exclusively. The court refused to admit the evidence, stating that “evidence that the [defendants] had not restrained the commerce of some dealers would not . . . disprove the affirmative evidence that a conspiracy to restrain the trade of dealers had been formed.” 121 F.2d at 405.

179. Compare notes 379-410 infra and accompanying text.


In other cases, § 3 violations have been found when dealers received special discounts for dealing exclusively. Carter Carburetor Corp. v. FTC, 112 F.2d 722 (8th Cir. 1940); United States v. Linde Air Prods. Co., 83 F. Supp. 978 (N.D. Ill. 1949); Maguire Industries, TRADE REG. REP. (1957-1958 FTC Cas.) ¶ 27446 (1958) (also Robinson-Patman Act violation). But cf. Lipson v. Socony-Vacuum Corp., 87 F.2d 265 (1st Cir.), cert. granted, 300 U.S. 651, cert. dismissed, 301 U.S. 711 (1937); Shell Oil Co., 3 TRADE REG. REP. ¶ 27762 (FTC Feb. 5, 1959). See notes 534-37 infra and accompanying text.

181. 217 F.2d 821 (2d Cir. 1954), affirming 50 F.T.C. 281 (1953).

182. 217 F.2d 867 (7th Cir. 1954), affirming 50 F.T.C. 681 (1954).
twenty-two per cent of "the nation's choicest retail outlets for hearing aids" and two million dollars worth of annual sales via requirements contracts. The Second Circuit accepted the FTC position that the rule of Standard Stations compels "a finding of unlawful conduct under section 3... [once it has been shown that] competition has been foreclosed in a substantial share of the line of commerce affected." The court felt itself driven to this conclusion "even in the face of evidence tending to indicate that the number of competitors in a particular line of commerce has increased." Thus, respondent's attempt to show the absence of actual anticompetitive effect of and economic justification for its exclusive contracts was rejected. The substantial lessening of competition banned by the Clayton Act was conclusively presumed from the degree of market foreclosure.

Dictograph probably involved a situation in which the conclusion was justified that the quantity of commerce affected by exclusive dealing had a significant effect on competition. Parallel use of exclusive dealing contracts by the major hearing aid manufacturers may well have denied newcomers to the market access to well-established, trained, responsible, independent hearing aid distributors. These dealers were the "choice outlets." New entrants would then be forced to turn to less desirable outlets, such as optical, drug, and department stores. Such outlets probably entail higher unit selling costs for manufacturers who must distribute through them. These higher costs would bar fully effective competition by new entrants. To avoid suffering higher distribution costs than the established firms, entrants could train their own dealers. But this would require the investment of time and capital in

183. 217 F.2d at 826, 828. Neither court nor FTC gives the total market share foreclosed by parallel use of exclusive dealing contracts. However, a subsequent decision, Beltone Hearing Aid Co., 52 F.T.C. 830 (1956), asserts that there was nearly total foreclosure. Id. at 836.

184. 217 F.2d at 825. The court is quoting Standard Stations, 337 U.S. at 314.

185. 217 F.2d at 824.

186. See Beltone Hearing Aid Co., 52 F.T.C. 830 (1956).

187. 50 F.T.C. at 294-95.

188. The competitor Cleartone had 500 such outlets and 15 regular dealer outlets, each of which groups sold 50% of total Cleartone sales. See Beltone Hearing Aid Co., 52 F.T.C. 830 (1956). This represents about a 30 times better showing by dealer distributors. But note that Zenith, a major producer, relies on "inferior" outlets successfully. 50 F.T.C. at 295.

189. Dictograph originally had to do this. 217 F.2d at 824. However, that Dictograph could do this at an earlier stage of the hearing aid industry's development is no reason to believe that this is equally feasible now. Possibly, the early entrants to the industry were at no cost disadvantage with respect to one another when they all had to incur the same training program-expenses. But now, an entrant forced to meet current price levels might not be able to absorb the cost of carrying so large an investment.

Query: Does the firm which invests in a training program "deserve" a reward in the form of an exclusive dealing arrangement so as to have an incentive for its efforts? Or is the reward from the first use of the trained outlets enough? Cf. U.S. Const. art. I, § 8 (patents and copyrights); Stern, Buyer Indifference and Secondary Meaning in Trademark and Unfair Competition Cases, 32 Conn. B.J. 381, 396-97 & nn.46, 47 (1958).
a training program. Thus, the exclusive dealing system probably imposed barriers to the entry of effective new competition into the hearing aid industry, either in the form of a higher distribution cost barrier, or a training cost barrier plus a time delay. Consequently, it appears that Dictograph's application of the rule of *Standard Stations* can be economically justified.

The vertical integration system, however beneficial to the integrating firm, would not, if these barriers in fact existed, have been consistent with the preservation of effective competition in the industry.

Between the time the Commission decided Dictograph and its counsel argued the appeal before the Second Circuit, the *Maico Co.* decision was handed down. And in *Maico*, the Commission changed directions and expressly rejected the quantitative substantiality rule of *Standard Stations*. An initial hearing examiner had declared Maico's requirements contract integration system of hearing aid distribution in violation of section 3, stating that "there must have been lessening of competition because respondent [was] the 'fourth, fifth, or sixth' largest company in the hearing-aid field" and had enjoyed annual sales of nearly two million dollars. Evidence concerning the lack of actual anticompetitive effect of the distribution system had been excluded, in accordance with the rule in *Standard Stations*. On appeal, the Commission reversed the initial order, directing the examiner to hear and evaluate the excluded evidence.

The *Dictograph* case tells us that Maico was in an industry whose marketing practices may appropriately be described as amounting to collective foreclosure. The inference would not be farfetched that Maico's requirements contracts created a significant clog on competition and helped prevent late arrivals from wresting away more than an insignificant portion of the market. Nevertheless, the Commission did not feel bound to rely upon such inferences. First, it did not believe, as did the Court in *Standard Stations*, that such an economic investigation would stultify the Clayton Act's legislative mandate.

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When this defense was invoked in the Outboard Marine & Mfg. Co., 52 F.T.C. 1553 (1956), and respondent suggested that newcomers should train their own dealers, the initial hearing examiner's view was:

> But that can be no justification for respondent foreclosing experienced and 'developed' dealers from its competitors or their distributors. The fact that the latter can go the longer and more expensive route is no answer to the law's evident command that they should have equal competitive opportunity to sell through all dealers, 'developed' as well as ignorant. Here they have been walled off from the best outlets and left to persuade and train newcomers.

*Id.* at 1575.


191. *Id.* at 486.


193. 50 F.T.C. at 487; see *Standard Oil Co. v. United States*, 337 U.S. 293, 313 (1949). The FTC interpreted "may" less inclusively than did Justice Frankfurter. It adopted a standard of actual or probable anticompetitive effect like that presented in the Jackson dissent.
Nor, apparently, did it agree that the investigation would prove inconclusive. Finally, although the investigation might be one "most ill-suited for courts," the Commission believed itself possessed of sufficient economic expertise to essay the task.

A reading of section 3 of the Clayton Act clearly indicates Congress intended to outlaw only those exclusive dealing agreements which are lessening or which if allowed to continue will probably lessen competition or tend to create a monopoly. We believe the structure of the Federal Trade Commission was specifically designed to make decisions involving this type of complex economic problem. To refuse to exercise our talents as an administrative tribunal in these cases because the courts feel "ill-suited" to weigh all of the relevant factors, would deprive the country of the very services which we were created to furnish.

In reaching this conclusion, the Commission relies on a footnote in the Frankfurter Standard Stations opinion:

The dual system of enforcement provided for by the Clayton Act must have contemplated standards of proof capable of administration by the courts as well as by the FTC and other designated agencies. Our interpretation of the Act, therefore, should recognize that an appraisal of economic data which might be practicable if only the latter were faced with the task may be quite otherwise for judges unequipped for it either by experience or by the availability of skilled assistance.

That it was Mr. Justice Frankfurter's intention to justify a dual standard for the dual system of enforcement is questionable. In any case, the Commission, since Maico, has pursued its own approach to the Clayton Act standard, one which departs, as it claims, from the quantitative substantiality test of Standard Stations.

Anchor Serum was the first Commission decision rendered under the new dispensation. Anchor was the largest of nine producers selling hog cholera serum to farmers and farmers' cooperatives. "Specific instances [were] shown . . . where the market for serum . . . [was] substantially foreclosed to producers other than petitioner by reason of the latter's requirements contracts."

194. See id. at 309, 314.
195. See ibid.
196. 50 F.T.C. at 488.
197. 337 U.S. at 310 n.13.
199. In a recent § 7 horizontal merger case, Brillo Mfg. Co., TRADE REG. REP. (1957-1958 FTC Cas.) ¶ 27242 (1958), the FTC reversed and remanded the decision of an initial hearing examiner who had followed a "quantitative substantiality" rule to find a violation on one count and a "quantitative insubstantiality" rule to dismiss a second count. The case was remanded to the examiner and he was directed to consider actual competitive effects in both situations. See Comment, 68 YALE L.J. 1627, 1649-63 (1959).
200. Anchor Serum Co. v. FTC, 217 F.2d 867, 872 (7th Cir. 1954).
with an Iowa and an Illinois co-op. Before Anchor instituted the exclusive contractual arrangements, a competitor, Lederle, sold these co-ops about 200,000 dollars worth of serum annually; afterwards, Lederle could make no sales to them.

It is evident that this competitor was completely stymied in its effort to do business with these two contract holders . . . because the latter were under obligation to make all their purchases from petitioner. A similar fate was met by the Diamond Serum Company, another competitor of petitioner. . . . It would require a naive mind to conclude, as petitioner would have us do, that the agreements under consideration could result in other than an adverse effect upon competition. . . . It thus appears plain that the products handled by petitioner's exclusive contract holders are removed from the competitive area.201

*Anchor Serum* is apparently a case of individual rather than collective foreclosure. Neither the Seventh Circuit nor the Commission alluded to the market effect, or even existence, of parallel arrangements. Moreover, the test of substantiality employed was apparently not market percentage, but dollar volume. The injury to competitors from which injury to competition was inferred was not foreclosure of a substantial portion of the market; rather, it was preemption of a substantial amount of sales to the detriment of those competitors who had previously enjoyed them.202 Since the size of the market share foreclosed by integration is not relied upon, this case would appear to come close to embracing the rule, attributed to *Standard Stations* by its critics,203 that a significant lessening of competition can be inferred whenever a "significant" (beyond *de minimis*, rather than "substantial") market share

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201. *Id.* at 873.

202. In addition to the injuries suffered by the two competitors, Lederle and Diamond, $200,000 and $100,000 of annual sales respectively, one more competitor was injured by Anchor's requirements contracts with the farmer co-ops. This competitor was Fidelity, who sold to drug stores in Illinois and Iowa. Fidelity's sales dropped from $42,000 to $14,000 a year because the drug stores were "unable to compete" with the co-ops under contract to Anchor. *Anchor Serum Co.*, 50 F.T.C. 681, 685-88, 690, aff'd, 217 F.2d 867 (7th Cir. 1954). Anchor's total sales under requirements contracts amounted to about $2 million a year. See 50 F.T.C. at 684.

203. See note 124 *supra* and accompanying text. It is submitted that the Anchor contracts, on the basis of the sparse evidence relied upon in the decisions, properly belong in the gray, "not proved" zone. See text following note 130 *supra*.

A recent case that may be open to the same criticism is *United States v. Sun Oil Co.*, TRADE REG. REP. (1959 Trade Cas.) ¶ 69398 (E.D. Pa. July 1, 1959). At the time the suit was commenced, Sun was the twelfth largest oil company in the United States and sold 8% or 9% of the relevant market. Brief for United States, p. 9.

The government case was not premised on the theory of collective, although not collusive, market foreclosure. Brief for United States, *passim*. Both the Justice Department and the court focused on the absolute number of dealers affected (6500), and the dollar volume of commerce involved. This approach harks back to *International Salt Co. v. United States*, 332 U.S. 392, 396 (1947) ("not insignificant"). See text at note 126 *supra*. 
is foreclosed. In any case, the move to injury to competition from injury to competitors required a greater leap than it did in *Standard*.\textsuperscript{204}

While the *Maico* case has been enthusiastically greeted as a retreat from quantitative substantiality,\textsuperscript{205} such enthusiasm may prove premature. In the cases since *Anchor Serum*, the Commission has frequently turned its back on the rule of *Standard Stations*, but the rule it has espoused in place of quantitative substantiality is pure "injury to competitors." It is readily apparent that this rule is far more unfavorable to defendants than quantitative substantiality, and the test of illegality it poses far more casual.

Among the post-*Maico* cases *Revlon Prod. Corp.*\textsuperscript{206} is particularly interesting because it seems to mingle the injury to competitors and injury to competition approaches, but does not emulate *Standard Stations* by attempting to synthesize the two. The following passage in the Commission's decision illustrates the two approaches:

Competitors shut off from respondent's jobbers by its agreements presumably can sell through the other jobbers in the area. However, respondent's jobbers are recognized as being among the best in the country. And the record shows that in some cases the only other outlets available

\[\text{204. Another issue in the case was the relevance of coercion. Anchor had argued that its customers had approached it to negotiate requirements contracts in order "to achieve assured continuity of... supply... and freedom from 'shopping' around..." 50 F.T.C. at 692. The Commission rejected the defense, declaring that "the tri-dimensional aspect of the situation was disregarded and the interests of the public and of those competitors...to whom injury ensued...were not considered." Ibid. On appeal, the Seventh Circuit agreed with the Commission:}

There was evidence that some of the contracts, perhaps all, were entered into as a result of negotiations initiated by the purchasers rather than by petitioner. From this premise it is argued that the terms were not imposed by the petitioner and that as a result there was no illegality, even though the contracts had the proscribed effect on competition. The Commission rejected this argument and so do we. Certainly there is nothing in the language of the Act from which it can even be inferred that two classes of contracts were contemplated, depending upon whether the contract was initiated by the seller or the buyer. We think it is a novel theory that the rights, liabilities and obligations of parties to a contract depend upon which of the parties propose it. And we think it immaterial whether the contract was for the benefit of the seller or the buyer. In any event, the determining factor is whether the contract had the proscribed effect.

217 F.2d at 870. Compare note 240 infra.

205. See, e.g., ATT'Y GEN. NAT'L. COMM. ANTITRUST REP. 142-44 (1955); Handler, Antitrust in Perspective 38-39, 44-46, 124-126 (1957); Hodson, Exclusive Dealing, in How To Comply With the Antitrust Laws 140, 148 n.52 (Van Cise & Dunn ed. 1954) ("Thus, exclusive arrangements may be approved by the Commission in instances where the courts would refuse to examine [economic evidence] and exonerate."). But cf. Handler, Annual Review of Antitrust Developments, 10 RECORD OF N.Y.C.B.A. 332, 341 (1955).

206. 51 F.T.C. 260 (final order), motion to reopen denied, id. at 466 (1954). Revlon was prosecuted for violating § 3 by integrating with exclusive dealing contracts 16% of the "1100 first-class beauty supply jobbers." Id. at 279. Revlon sold to 176 out of the 1100, 157 of whom had formal franchise contracts. It appears that second class outlets were poor credit risks. Id. at 265, 277.
to such competitors were of lesser quality, and that they were deprived of full coverage in the area involved as a result of respondent's agreements. Further, if these contracts are found to be legal, there is a very great likelihood that similar contracts will be put into use by respondent's competitors, further restricting the number of beauty supply jobbers available to the small cosmetic houses. The cumulative effect of such agreements could as effectively close the market to competitors as if one company monopolized all of the jobbers.\textsuperscript{207}

The authors submit that this is all "injury to competitors." Even the last two sentences, in which "cumulative foreclosure" is envisioned and effect on "the market" mentioned, appear to regard such foreclosure as unlawful because it injures the excluded competitors ("the small cosmetic houses") rather than because it ultimately injures the public in the form of higher prices, poorer goods, or decreased output. Thus, on a motion to reopen the case because a new competitor had emerged as a leading national contender to Revlon, the Commission held the proffered evidence inconclusive, since it did not affect the finding that the exclusive dealing contracts had a "substantial restrictive effect on smaller competitors who, [unlike Hazel Bishop, did] not have sufficient resources to spend millions for advertising or to establish a complete jobber setup for their products from coast to coast."\textsuperscript{208}

The Commission might have justifiably concluded that the enormous expenditures by Hazel Bishop proved that Revlon had erected substantial barriers to the entry of new competition.\textsuperscript{209} But the Commission was not content to rely on injury to competition in the abstract. Instead, it observed that the Clayton Act is concerned with helping small business, and because the power of smaller companies to compete is adversely affected, a section 3 violation existed.\textsuperscript{210} Although this might be interpreted to be the language of "injury to competition," the thrust of the Commission's opinion seems to be "injury to competitors."

Perhaps a break with the injury to competitors rationale may be found in \textit{Outboard Marine \& Mfg. Co.}.\textsuperscript{211} Outboard, the dominant small boat motor manufacturer,\textsuperscript{212} did not allow its dealers to carry other marine motors. Since dealers preferred to carry a full line of motor sizes,\textsuperscript{213} those competitors of Outboard who manufactured only short lines of motors were unable to secure access to many first class outlets.\textsuperscript{214} The FTC initial examiner found that "it

\textsuperscript{207} Id. at 279. This passage suggests the possibility that higher costs were imposed on competitors. If the case were to be economically justified at all, it would require reliance on the "incipiency doctrine," see note 276 infra, since only 16% of the market was affected.

\textsuperscript{208} 51 F.T.C. at 468.

\textsuperscript{209} For discussion of barriers to entry created by advertising, see \textit{Bain} 114-43. See also American Tobacco Co. v. United States, 328 U.S. 781, 797 (1946).

\textsuperscript{210} 51 F.T.C. at 468.

\textsuperscript{211} 52 F.T.C. 1553 (1956).

\textsuperscript{212} Outboard sold over 50% of all outboard motors. Id. at 1554.

\textsuperscript{213} Id. at 1569, 1572.

\textsuperscript{214} Ibid.
cost a capital outlay of $1,500,000 to produce one size motor . . . and $350,000 to add one more size.” 215 Had Outboard not foreclosed so many outlets to competitors, entry with a partial range of motor sizes might have been feasible. But Outboard’s dealing policy forced competitors to produce a full line or else fall back on second-rate distributors. 216 The choice was between a large capital outlay or high distribution costs. 217 Moreover, the examiner found that it took from one to three years to develop a new dealer to the point where he became “satisfactory.” 218 It is quite likely that this time lag discouraged entry of competition into the industry. Nevertheless, the examiner assumed that no injury to competition occurred, 219 and he condemned Outboard solely for injuring competitors. In affirming the initial order, however, the Commission seemed to return to quantitative substantiality: “The trial record fully supports a conclusion of probable injury to competition through the foreclosure of competitors from a substantial and highly desirable portion of the outboard motor market.” 220

Thus, in the various post-Maico cases, the extent of the Commission’s

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215. Id. at 1576.

An extreme example of a single manufacturer foreclosing the greater part of available outlets for competitors is found in Harley-Davidson Motor Co., 50 F.T.C. 1047 (1954). The dominant heavy motorcycle manufacturer refused to permit his dealers to carry any other lines. The competitor Simplex, who manufactured only lightweight motorcycles, was thus denied access to 80% of the potential market for his product. Id. at 1057. (Query: Does this mean 80% of potential outlets or 80% of potential sales volume?) Simplex’s sales dropped to 25% of its former volume as a result of the policy.

Evidence indicated that dealers would have preferred to retain Simplex had Harley Davidson permitted this. Id. at 1058-59. But when confronted with the choice between Harley-Davidson’s full line and Simplex’s short line, “the cold facts of business and analization [sic] of potential markets . . . [forced dealers] to remain with Harley because of the increased demand for large motorcycles.” Id. at 1058. Whether or not Harley-Davidson’s policy actually maximized its revenues, see Bowman, Tying Arrangements and the Leverage Problem, 67 Yale L.J. 19, 20-21 (1957), it does seem that the policy inhibited competition. In condemning Harley Davidson’s policy the Commission does seem to have been concerned with effects on competition rather than on competitors alone. See 50 F.T.C. at 1056.

217. See text at note 189 supra.

219. “There is no evidence that the buying public had any difficulty in finding dealers from whom to buy motors manufactured by competitors of respondent, and the fact is so found.” Id. at 1574. The authors read this statement to be a finding of the availability of comparable motors at “reasonable” prices (i.e., prices which would obtain under a regime of workable competition), rather than a finding that competitors’ motors can be found without difficulty, but at a high price.

220. Id. at 1579.
economic analysis for the determination of actual anticompetitive effect has frequently been to specify instances of injury to individual competitors. One who agrees with Mr. Justice Jackson in *Standard Stations* and considers it farfetched for the Court to find significant injury to competition from foreclosure of a substantial share of the market cannot then take consolation in an "economic analysis" which finds injury to competition from bare injury to specific business rivals. The authors prefer the view of Professor Adelman:

From the observation that certain forms of integration can hurt competition by hurting certain competitors it had been fatally easy to slip into the habit of looking simply to the effect on competitors as the criterion. . . . Integration is always and necessarily an exclusion of competitors. Whether it is also an exclusion of competition . . . depends on the particular market situation. Absent a recognition of this principle, there must always be a chronic tendency under the antitrust laws toward making exclusion [of competitors]—and therefore integration—illegal *per se*. . . . So long as we have effective competition, however, there will be disgruntled competitors and pressures toward soft competition.

The authors suggest that the rule of *Standard Stations* is far preferable to a flat "injury to competitors" rule. Emphasis on injury to competitors as the wrong forbidden by the Clayton Act, rather than injury to the general purchasing public, may well develop into a standard of legality which will prevent effective competition by denying business the benefits of integration. Although the post-*Maico* cases may be reconcilable with an injury to competition approach, the Commission's dominant theme seems to be injury to competitors.

221. In addition to the cases discussed in text, *supra*, see Beltone Hearing Aid Co., 52 F.T.C. 830 (1956), where an exclusive dealing contract system was enjoined because of (1) injury to dealers who submitted to the contracts and lost the opportunity to sell competitive products, (2) injury to dealers discontinued because they refused to submit to the contract integration system, (3) injury to competing manufacturers, and (4) suppression of free and open competition. 52 F.T.C. at 841-42.

A possible break with the injury-to-competitors rationale, and perhaps a return to *Standard Stations*, may be detected in two recent trial-examiner decisions. General Mills, Inc., 3 TRADE REG. REP. ¶ 28201 (FTC Aug. 21, 1959); The Ice Cream Cases [Carnation Co., No. 6172; Borden Co., No. 6173; Beatrice Foods Co., No. 6174; National Dairy Products Corp. No. 6175; Pet Milk Co., No. 6176; Fairmount Foods Co., No. 6177; Arden Farms Co., No. 6178; Foremost Dairies, Inc., No. 6179; H. P. Hood & Sons, No. 6425] FTC, June 26, 1959.


223. *Cf.* Adelman, *supra*, note 222, at 305 ("... the test of share of the market is at least a first and wavering approximation to degree of market control.").

To the extent that the cost reductions which integration makes possible are passed on to the consumer in the form of lowered prices, the public benefits from integration. But even when such savings are not passed on in the form of lowered prices, the public benefits in the long run, at least to some degree, from the release of capital or factors of production for allocation elsewhere in the economy, even if public benefit is not at its maximum. See Boulding, *Economic Analysis* 607-08 (3d ed. 1955).
and no reason exists to anticipate that future cases will be compatible with a market injury standard.\footnote{224}

**MPAS: Sherman-Clayton Coalescence?**

Section 3 of the Clayton Act declares unlawful the sale of goods or other commodities on the condition or understanding that the buyer is not to deal in the goods of a competitor of the seller. Conditions imposed on the seller, however, are not within the language of the statute, and accordingly output contracts are immune from section 3.\footnote{225} Moreover, restrictive contracts for the sale of anything which is not a “commodity” are outside the scope of the Act.\footnote{226} The problems created by the narrow wording of section 3 are strikingly illustrated in the \textit{MPAS} case.\footnote{227}

Like \textit{Standard Stations}, \textit{MPAS} deals with an oligopolistic industry—in this case film advertising. Along with newsreels, cartoons, and coming attractions, \textit{MPAS} deals with an oligopolistic industry—in this case film advertising. Along with newsreels, cartoons, and coming attractions, ...
advertising films precede the main feature in 12,000 of the nation's 20,000 motion picture theaters. Advertising films differ from others, at least as far as the theater owner is concerned, in that they reverse the usual flow of revenue: while the theater owner must pay to show other films, he is paid to show advertisements.\textsuperscript{228} The producers of advertising films buy time from theaters for resale to advertisers. For each advertiser the producers select an appropriate film from their "library," splice in appropriate "personalizing" captions at start and finish, and then turn the film over to theaters for projection.\textsuperscript{229} When the FTC took action against \textit{MPAS} and the other three leading producers of advertising films\textsuperscript{230} seventy-five per cent of the 12,000

\textit{Diversified Servs., Inc.}, 102 F. Supp. 645 (D. Minn. 1951) (money not \textit{cjusdem generis} with "goods, wares . . .").

But when the sale or lease of the non-commodity is closely coupled with a sale of goods, as in a patent tie-in (\textit{i.e.}, a chose in action is conveyed on condition certain goods be bought only from the seller of the chose), there may be a violation. Lord v. Radio Corp. of America, 24 F.2d 565, 567-68 (D. Del.), aff'd, 28 F.2d 257, 259-61 (3d Cir.), \textit{cert. denied}, 278 U.S. 648 (1928). Patent tie-ins are subject also to the patent misuse doctrine, \textit{i.e.}, a patent may not be utilized in a way which conflicts with the policy of the antitrust laws. The development and expansion of this doctrine has been influenced by the public policy declared in \textit{Clayton Act} § 3. Morton Salt Co. v. G. S. Suppiger Co., 314 U.S. 488 (1942); Carice Corp. of America v. American Patents Dev. Corp., 283 U.S. 27, 34 n.4 (1931); Motion Picture Patents Co. v. Universal Film Mfg. Co., 243 U.S. 502, 517 (1917). The foregoing case law may largely have been superseded by \textit{Northern Pac. Ry. v. United States}, 356 U.S. 1 (1958), which declares illegal per \textit{se} under § 1 of the Sherman Act \textit{all} tie-ins with greater than \textit{de minimis} effect. But the principle that § 3 extends to transactions even touching commodity sales remains of interest.

A further exception to § 3 is found in requirements contracts for patented, copyrighted, or trademarked goods. The requirement that the purchaser buy all his needs of the goods over which the vendor has a lawful monopoly is said not to fall afoul of the antitrust laws because there is no attempt to extend the scope of the monopoly into an unprotected area: moreover, for the purchaser knowingly to secure any of his needs from an infringer would itself be unlawful, and therefore a contract requiring that he not do this is said to be perfectly reasonable. Nor is it misuse or abuse of the monopoly to grant a license over only part of the monopoly power (copyright: print, publish, copy, vend, exhibit, perform, represent, produce; patent: make, use, vend). Steiner Sales Co. v. Schwartz Sales Co., 98 F.2d 999, 1007-11 (10th Cir. 1939), \textit{cert. denied}, 305 U.S. 662 (1939); Baldwin-Lima-Hamilton Corp. v. Tatnall Measuring SysSy Co., 169 F. Supp. 1, 25, 26 (E.D. Pa. 1958), aff'd \textit{per curiam}, 268 F.2d 395 (3d Cir. 1959); Cardinal Films, Inc. v. Republic Pictures Corp., 148 F. Supp. 156, 157-59 (S.D.N.Y. 1957).

\textsuperscript{227} \textit{FTC v. Motion Picture Advertising Serv. Co.}, 344 U.S. 392 (1953), \textit{reversing} 194 F.2d 633 (5th Cir. 1952), \textit{affirming} 47 F.T.C. 378 (1950).

\textsuperscript{228} "Features, news reels and shorts cost [the theatre owner] money. However, trailer ads actually reverse the flow of film money back into his own till. He pays for a film of somebody's love life, but he gets paid for showing the cold facts about somebody's breakfast food or shaving mugs." Reid H. Ray Film Indus., 47 F.T.C. 326, 342 (1950) (dissenting opinion).

\textsuperscript{229} \textit{MPAS}, 47 F.T.C. at 385, 391.

\textsuperscript{230} See Reid H. Ray Film Indus., 47 F.T.C. 326 (1950); Alexander Film Co., 47 F.T.C. 345 (1950); United Film Ad Serv., Inc., 47 F.T.C. 362 (1950).
theaters in the country which show these films had exclusive dealing contracts with one of the Big Four. This was not respondents' first bout with the Commission; in a previous encounter, a cease and desist order had been issued forbidding them from conspiring together to fix their prices.

Once again the FTC issued cease and desist orders against each of the four. The maximum term for their exclusive contracts was limited to one year. Contracts of duration up to a year were allowed because of the economic advantages a reasonable degree of vertical integration offered the parties, but the existence of longer arrangements was deemed anticompetitive. The Supreme Court, over a vigorous dissent by Mr. Justice Frankfurter, affirmed the Commission's order.

MPAS could not have been brought as a Clayton Act case: first, theater time is not a commodity, and, second, there was no sale on condition that the buyer (MPAS) was not to deal in the goods of other sellers (the theater owners). Nevertheless, Mr. Justice Douglas, writing for the Court, accepted

231. There were approximately 20,305 theaters in the country, of which about 12,676 exhibited advertising films. MPAS had exclusive contracts with 2,493 in 27 states. 47 F.T.C. at 386. MPAS had, then, 20% of the national market and 40% of the 27 state local market under exclusive contracts. Of the other leaders, Alexander had exclusive contracts with 4,913 theaters or 40% of the national market, United had 1,562 or 12%, and Ray had 458 or 4%. Id. at 386-87. In some states MPAS controlled as much as 70 to 75% of the market under exclusive contracts. Brief for FTC Before Supreme Court, pp. 18-19.

232. Screen Broadcast Corp., 36 F.T.C. 957 (1943). Both rates to be paid by advertisers and to exhibitors were fixed.

233. Not all the exclusive contracts used by the Big Four had exceeded one year in duration. 344 U.S. at 393-99 (dissent); Hodson, Exclusive Dealing, in How To Comply With The Antitrust Laws 140, 147 (Van Cise & Dunn ed. 1954).

234. "The Commission . . . concluded that, although the exclusive contracts were beneficial to the distributor and preferred by the theater owners, their use should be restricted in the public interest. The Commission found that [one-year contracts] . . . would not be an undue restraint upon competition, in view of the compelling business reasons for some exclusive arrangement." 344 U.S. at 395-96. See also id. at 396 n.2. This language appears to be an attempt to reconcile the "good business reasons" and "public injury" tests. See text at notes 87, 88 supra. Is this a retreat from the unqualified position of Standard Stations? "[I]t would seem unimportant that a short run by-product of stability may have been greater efficiency and lower costs, for it is the theory of the antitrust laws that the long-run advantage of the community depends upon the removal of restraints upon competition." 337 U.S. at 309. In this connection it should be remembered:

(1) In MPAS the Supreme Court did no more than affirm an FTC order permitting one-year contracts; it did not allow one-year exclusive contracts, sua sponte.

(2) The Court in Standard Stations may have been motivated by the belief that the contracts involved were actually "perpetual." See note 138 supra and accompanying text. Compare United States v. American Can Co., 87 F. Supp. 18, 31 (N.D. Cal. 1949) (allowing one-year contracts).

235. The seller is the theater proprietor who binds himself not to sell to anyone else "the privilege of boring the public" with film advertisements, which is the "theater
the position urged by the Solicitor General that the rule of Standard Stations was appropriate to the case. The majority treated the integration system as if they were dealing with requirements contracts instead of output contracts. And possible formalistic distinctions between forward and backward integration by contract were disregarded.

The Commission found in the present case that respondent's exclusive contracts unreasonably restrain competition and tend to monopoly. Those findings are supported by substantial evidence. This is not a situation where by the nature of the market there is room for newcomers, irrespective of the existing restrictive practices. The number of outlets for the firms is quite limited. And due to the exclusive contracts, respondent and the three other major companies have foreclosed to competitors 75 percent of all available outlets for this business throughout the United States. It is, we think, plain from the Commission's findings that a device owner's inalienable right . . ." Reid H. Ray Film Indus., 47 F.T.C. 326, 342 (1950) (dissenting opinion). Thus, the restrictive sale is in the wrong direction for the Clayton Act to apply.

The majority was well aware that this was not a Clayton Act § 3 case. 344 U.S. at 397.

Section 3 of the Clayton Act reflects a strong public policy against exclusive dealing arrangements. That section fatally prohibits such agreements by buyers of goods where the effect may be to substantially lessen competition . . . [citing Standard Stations and Richfield]. Although the contracts in the instant case are presumably not within Section 3 since the exclusive commitment is by the seller of screen space (the theater) rather than by the buyer (respondent), the effect on competition is the same in either situation. The basic public policy against exclusive dealing arrangements which adversely affect competition, as declared by Section 3 of the Clayton Act, bring respondent's exclusive contracts within the Commission's authority to prohibit unfair methods of competition.

Id. at 13. Note that the majority opinion does not directly cite Standard Stations, although the dissent does.

Careful study of the Court's opinion indicates that it was willing to go beyond the position urged by the Solicitor, and hold the contracts in violation of § 1, and therefore in violation of § 5, rather than in violation of § 5 even though not in violation of § 1. See Handler, Antitrust in Perspective 126, n.51 (1957) ("Although the Supreme Court actually found that the exclusives at issue violated the Sherman Act, it indicated by way of dictum that the Commission might have been entitled to relief under Section 5 of the Federal Trade Commission Act, even if it had not been able to prove a violation of either the Sherman or Clayton Act.").
which has sewed up a market so tightly for the benefit of a few falls within the prohibition of the Sherman Act and is therefore an "unfair method of competition" within the meaning of § 5(a) of the Federal Trade Commission Act.\textsuperscript{238}

To Justice Frankfurter, the Standard Stations rule urged by the Solicitor General\textsuperscript{239} and accepted by the Court would be inappropriate in a Sherman Act case. In his view, imputing the total market effect of parallel exclusive dealing arrangements to each user is appropriate only in actual conspiracy cases or in Clayton Act cases. "While the existence of the other exclusive

\begin{enumerate}
\item \footnotesize\textsuperscript{238} 344 U.S. at 395. (Emphasis added.) It may be noteworthy that the language used by the majority opinion "unreasonably restrain competition and tend to monopoly" shows a blending of the phraseology employed in § 1 of the Sherman Act and in the Clayton Act. Moreover, "tend to monopoly" is similar to both "tend to create a monopoly" in the Clayton Act and "monopolize or attempt to monopolize" in the Sherman Act § 2.
\item \footnotesize\textsuperscript{239} As is seen from note 236 \textit{supra}, the Solicitor General urged that the Court adopt the "substantial foreclosure" test of Standard Stations. The interpretation of Standard here urged appears to be the 65% or 76% collective foreclosure rather than the 6.7%, 16% or even 23% fractions also involved in that case. Moreover there is no reliance on gross dollar volumes at all.
\end{enumerate}

Here the Commission has found that respondent's long-term exclusive dealing contracts unreasonably restrain competition and tend to monopoly. That finding is supported by a showing that respondent, in the 27 states in which it operates, has exclusive contracts with almost 40% of the theaters exhibiting advertising films, and that the four major companies, against all of whom the Commission entered cease and desist orders, together had exclusive contracts with 75% of all available outlets throughout the United States. In view of the highly limited number of opportunities for displaying advertising films it is obvious that such a situation enables the established companies "collectively, even though not collusively, to prevent a late arrival from wresting away more than an insignificant portion of the market." \textit{Standard Oil Co. v. United States}, 337 U.S. 293, 309.

Brief for Petitioner, p. 13.

The Commission found that the effect of respondent's exclusive contracts in limiting the outlets for advertising films was increased by the like exclusive contracts made by the three other principal companies in the business. The four major concerns, together, foreclosed to other companies 75% of all available outlets throughout the United States, and, as indicated above, undoubtedly the foreclosure of the more desirable available outlets ran considerably higher. When, as here, the four dominant concerns in the industry pursue the same restrictive practices, the limitations on competition which result are compounded. In \textit{Standard Oil Co. v. United States}, 337 U.S. 293, 309, this Court observed that, since all the major suppliers had been using requirement contracts, it would not be far fetched to infer that the effect has been to enable the established suppliers "collectively, even though not collusively, to prevent a late arrival from wresting away more than an insignificant portion of the market.

\textit{Id. at 20.} (References to record omitted.) See also MPAS, 47 F.T.C. at 391 ("injurious effects . . . increased by the cumulative effects of similar agreements"). Note, the over 75% of outlets in MPAS is strikingly close to the 76% of Standard Stations. See text at note 98 \textit{supra}.
contracts is, of course, not irrelevant in a market analysis, see Standard Oil Co. v. United States, 337 U.S. 293, 309, this Court has never decided that they may, in the absence of conspiracy, be aggregated to support a charge of Sherman Law violation. Cf. id., at 314."

Is this criticism of the majority opinion justified? In Standard Stations, Justice Frankfurter had no difficulties in aggregating contracts in the absence of a conspiracy. In order to evaluate the competitive effect of Standard's contracts, the Court had to consider the market setting in which they occurred. It was the word "effect" in the statutory phrase, "where the effect may be to substantially lessen competition," which justified aggregation; the incipiency word "may," peculiar to the Clayton Act, was not the basis for aggregation, but for the jump from quantity to quality. Nor is there any need to resort to a conspiracy doctrine in order to aggregate. Testing contracts in their whole business setting is the very essence of the Sherman Act rule of reason. According to that general test, restrictive agreements are banned whenever they are intended to have, or in fact have, a significant anticompetitive effect—this being measured in terms of price, output, or quality of goods. Thus, in MPAS, it was essential to evaluate the effect of respondents' contracts in their whole business setting in order to determine whether they passed the Sherman Act test.

MPAS appears to reveal the use of vertical integration by exclusive dealing contract to bolster horizontal power. It seems clear that the Big Four

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240. 344 U.S. at 399-400. The dissent also asserts that the facts found by the Commission do not bring the respondent within the Standard Stations rule. Id. at 401-03. In MPAS, in contrast to Standard Stations, there was no coercion by respondent. First, "the obvious bargaining power of the seller vis-a-vis the retailer" was absent, and second, there was evidence in the Commission's findings that theaters often demand exclusive arrangements. Id. at 402. Justice Frankfurter asserted that in Standard Stations "we recognized the discrepancy in bargaining power and pointed out that the retailers might still insist on exclusive contracts if they wanted. See 337 U.S., at 314." Ibid. However, the page cited reveals only the statement that requirements contracts would be superfluous if they were really economically desirable for service stations, because then the stations would buy all their needs from a single supplier without being bound to do so by a contract, and might indeed secure firm offers from suppliers for their requirements "without binding them[elves] to refrain from looking elsewhere." Compare note 204 supra.

The majority opinion does not meet this criticism squarely. It gives the reply that the Commission considered this argument but found that the use of the agreements "should be restricted in the public interest," a finding within the limits of the Commission's "allowable judgment." 344 U.S. at 395-96.

241. This is the test of Apex Hosiery Co. v. Leader, 310 U.S. 469, 493, 500, 512 (1940), the leading case on the definition of "unreasonable" under § 1. This test is followed in Times-Picayune Publishing Co. v. United States, 345 U.S. 594, 614-15 (1953); United States v. Columbia Steel Co., 334 U.S. 495, 525, 527 (1948); accord, United States v. International Harvester Co., 274 U.S. 693, 707-08 (1927); Board of Trade v. United States, 246 U.S. 231, 238 (1918); see United States v. Aluminum Co. of America, 148 F.2d 416, 424 (2d Cir. 1945) ("invariably affects prices or is intended to do so").
producers had considerable power over the price of film advertising. The best indication of this is that they had exerted it in the past.\textsuperscript{242} Another indication of their strength is the share of the market they controlled—seventy-five per cent. And this figure is an average market share. In some markets, MPAS alone possessed a near monopoly.\textsuperscript{243} It is highly probable, although data are lacking on this point, that in still other areas of the country, MPAS and other members of the Big Four together possessed monopoly power.\textsuperscript{244}

Monopoly power at both levels of the operation, i.e., at the theaters and at film production seems necessary to guarantee the enjoyment of the fruits of this particular monopoly. The basis of power over price in the local advertising market is control of the limited number of local theaters.\textsuperscript{245} He who controls the theaters is in the position to enjoy the benefits of monopoly power in the business of selling film ads, or, at the least, to wield countervailing power against any advertisement producer monopolist and force him to share the monopoly “take.” Strategically, then, even in the absence of other considerations, MPAS had to integrate the theaters to assure itself protection against another’s seizing the opportunity. Moreover, it is probable that the advertising film producer is the person in the best strategic position to organize the monopoly,\textsuperscript{246} and the person least likely to be forced into sharing the monopoly revenues with the theater owners.\textsuperscript{247}

The collective control of the Big Four of over seventy-five per cent of the national market may have “sewed up a market so tightly” that entry by new-

\textsuperscript{242} See Screen Broadcast Corp., 36 F.T.C. 957 (1943).
\textsuperscript{243} See note 231 \textit{supra}. The relevant market for power over price exacted from advertisers would appear to be quite local. The radius of travel that a patron will go to see a movie would seem to define this market. Compare the nation-wide relevant market for economies of scale to the producer, who can mail his wares anywhere in the country, note 251, \textit{infra}.

\textsuperscript{244} Whether the Big Four exercised their power over price by following consciously parallel policies or by actual agreement is, it is submitted, immaterial. Moreover, under the philosophy of \textsection 2, it would be irrelevant even whether the Big Four had exerted their power, so long as they acted to maintain it. \textit{Att'y Gen. Nat'l Comm. Antitrust Rep.} 56 (1955).

\textsuperscript{245} Moreover, the screen time available in each theater is limited by the amount the patrons will tolerate. MPAS, 47 F.T.C. at 387; Record vol. 2, p. 10.

\textsuperscript{246} Perhaps an owners' cooperative booking agency would be another possibility, at least until the Justice Department started a Sherman Act prosecution for price fixing.

\textsuperscript{247} The bargaining power of the theater proprietor is usually weak because of the economic necessity to him of advertisement revenue, "... a sort of subsidy to keep the marginal operator alive." Reid H. Ray Film Indus., 47 F.T.C. 326, 342 (1950) (dissenting opinion). In this connection it is interesting to note that the large Interstate Circuit Theater chain realized that substantial profits could be made from dealing directly with advertisers; accordingly, it pulled its theaters out of the exclusive dealing integration system and handled its film advertisements on its own. Record, vol. 2, pp. 186-88. However, Interstate eventually gave the venture up and abandoned all screen advertising. During the period that Interstate used its ownership integration system, it did not produce all its own films, but rented some from the MPAS and Alexander libraries. \textit{Id.} at 188-89.
This industry appears to be characterized by economies of scale. Each producer requires a library of shorts which can be tailored to an individual advertiser's needs by splicing in his name at the beginning or end of the film. Clearly, the unit cost of the library decreases with the number of times each short is used, since the marginal cost is only the price of the name clips and perhaps an extra print of the ad strip. If a prospective entrant cannot hope to use his library intensively, he must anticipate high unit costs. Thus, collective control by the Big Four of over seventy-five per cent of the available market to producers may have effectively barred entry. The uncommitted twenty-five per cent may be too "thin" a market to attract entry. If the volume attainable from whatever share of the remaining twenty-five per cent a new competitor can secure is insufficient to cover his library costs, then he will not enter. Furthermore, the use of long term contracts with theaters isolates them from the market more effectively and lengthens break-in time for an entrant.

Given this business setting, the MPAS case reveals, minimally, a potential restraint on competition which, given a Clayton Act prosecution, would be within the scope of "may" as interpreted by Standard Stations. Probably, the restraint can even be considered a "full blown one." Thus, the decision probably furthers the cause of free competition. Some, however, might share the misgivings of the Frankfurter dissent about the Commission's lack of discerning economic analysis or failure to enunciate standards by which potential anticompetitive effect is to be judged. In Frankfurter's view, that seventy-five per cent of the market was covered by similar exclusive contracts, "does not automatically bring the accused arrangement within the prohibitions of" the Sherman Act and the Commission, echoed by the Court, "merely states a dogmatic conclusion that the use of these contracts constitutes an 'unreasonable restraint and restriction of competition.'"

The dissent appears to object, not only to aggregation of various firms' contracts, but to the very idea that effect on competition may be inferred from quantitative share of the market affected. Underlying this position is

248. 344 U.S. at 395.
249. See MPAS, 47 F.T.C. at 385, 391.
250. Ibid.
251. The relevant market with respect to economies of scale is that accessible to producers. Since transportation costs of the product are relatively low—films are light in weight—any producer can sell anywhere in the country. For example, MPAS has offices in New Orleans, but it supplies advertising films to the theater in the Connecticut town in which one of the authors lives. See also note 231 supra.
252. There is, however, evidence that MPAS and Alexander were willing to rent films from their libraries to at least one outsider. Record, vol. 2, pp. 188-89.
253. Compare text at notes 189, 218 supra.
254. See 344 U.S. at 394-95.
256. 344 U.S. at 399.
the absence of "may" language in the Sherman Law. The majority never replies to this objection.

However, can the case be justified on the doctrinal level? It may be tempting to explain the majority opinion in terms of reliance on section 5 of the FTC Act. Under such an interpretation, it is the latter act which harmonizes the Sherman and Clayton Act standards. But such a narrow interpretation is not warranted in the light of the explicit language of the majority opinion that the contract system "falls within the prohibitions of the Sherman Act and is therefore an 'unfair method of competition' within the meaning of § 5 . . . ."\textsuperscript{257} If MPAS is to be justified at all, it must be on the basis of the Sherman Act.

The Sherman Act proscribes restrictive agreements whenever they are intended to have, or in fact have, anticompetitive effects. Since the problem is to infer an anticompetitive effect from the share of the market affected by restrictive contracts, the actual effect branch of the rule is not available. That is, "effect" is the terminus of the inquiry, not its premise. Thus, the only conceptual tool available is the "intent" branch of the rule. Absent a conspiracy\textsuperscript{258} can intent, or even constructive intent, under the Sherman Act, carry the Court as far as "may" under the Clayton Act? The MPAS Court never chose to decide this question, since it allowed the FTC finding of anticompetitive effect to stand as a finding of fact rather than a legal inference subject to appellate review. Probably there is a residuum under the Clayton Act beyond the ambit of the Sherman Act "intent" test. But the lesson of MPAS appears to be that an "intent" test can go a long way towards "may." MPAS has eroded much of the imagined distinction between the Sherman and Clayton Act standards, at least in the vertical integration area.

Read together, Standard Stations and MPAS cover the most significant antitrust aspects of vertical integration by contract. First, they indicate a strong tendency in the Court to use essentially the same standards for forward or backward integration by contract—the policy of the Clayton Act is read into the Sherman Act\textsuperscript{259} and the narrow language of section 3 is not permitted to restrict the application of that policy. The unresolved question is—how complete will this Sherman-Clayton coalescence prove? Second, they demonstrate that the legality of an integration system is to be measured by the standard of market foreclosure. However, the courts have not determined whether "intent" permits as much of a move from quantitative share of the market affected to qualitative effect on competition as "may" does. Third, they teach that market foreclosure may be collective as well as individual. Thus, for any individual defendant who is one of the major firms in an industry where other majors use exclusive arrangements similar to defendant's, "restraint of trade" or "substantial lessening of competition" can be shown

\textsuperscript{257} Id. at 395.
\textsuperscript{258} Compare United States v. Socony-Vacuum Oil Co., 310 U.S. 150, 224 n.59 (1940).
\textsuperscript{259} Compare United States v. Columbia Steel Co., 334 U.S. 495, 507 n.7 (1948).
from the market effect of the aggregate of similar arrangements, even when they are not collusive.

260. An unresolved question in the cases is how "major" the firms using the exclusive arrangement must be before the collective foreclosure doctrine is appropriate. In Standard Stations, seven controlled 76% of outlets and sold over 65% of output. In MPAS, four controlled 75% of outlets. In FTC v. Cement Institute, 333 U.S. 683 (1948), a price fixing case, ten out of 74 respondent corporations controlled more than half of the 150 mills in the country, id. at 712-13. Probably, forty firms, each controlling about 2% of the market by vertical integration arrangements, would not be said to foreclose the market. But cf. Ray H. Ray Film Indus., 47 F.T.C. 326, 344 & n.1 (1950) (dissenting opinion). First, that there are forty "majors" is a symptom that the economy of scale barrier to entry problem is not acute. Therefore, a prospective entrant could probably succeed even though he could capture only a small share of the market. Here, not even a potential ("may") barrier to entry would exist. Second, the stability of a forty-member "oligopoly" is so uncertain that continued parallel action to bar entry is unlikely to occur. See note 160 supra. Where the boundary between forty firms in control of 80% of the market (probably lawful), and seven firms in control of 80% (probably unlawful) is located depends on the structure of the industry in question. See note 161 supra.

261. The collective foreclosure doctrine of MPAS and Standard Stations may also be viewed as a highly sophisticated version of conscious parallelism. See Interstate Circuit, Inc. v. United States, 306 U.S. 208, 226, 227 (1939). However, neither overt conspiracy nor conscious parallelism is relied upon in either opinion. Indeed, § 3 has no conspiracy requirement and in MPAS, a conspiracy under § 1 could not have been utilized because it would have been barred by res judicata. 344 U.S. at 397-98; see text at note 232 supra. Yet the two cases represent a further refinement of the doctrine. The aggregation of like contracts to measure their market effect is quite similar to the aggregation of like acts to infer intent to conspire. A corresponding evolution of conscious parallelism is seen in the Clayton Act § 2 context where individual use of a baring point system with knowledge that other sellers use it has been declared an unfair method of competition under § 5. Compare FTC v. Cement Institute, 333 U.S. 683, 708 (1948), with Triangle Conduit & Cable Co. v. FTC, 168 F.2d 175, 180-81 (7th Cir. 1948), aff'd per curiam by an equally divided Court sub nom. Clayton Mark & Co. v. FTC, 336 U.S. 956 (1949). See also FTC v. National Lead Co., 352 U.S. 419, 429-31 (1957). The majority was well aware that MPAS was not a Clayton Act § 3 case. 344 U.S. at 397. Note the majority opinion does not directly cite Standard Stations, although the FTC brief had relied upon that case, id. at 401; note 236 supra.


262. The Standard Stations Court followed the collective foreclosure route to a finding of violation of § 3 despite the fact that the Justice Department did not build its case around collective foreclosure. The Government relied, in its brief, pp. 46-47, only on one case on the point, Signode Steel Strapping Co. v. FTC, 132 F.2d 48, 54 (4th Cir. 1942), where the court had held, with respect to a tie-in policy used by the leading packaging industry firms:

[T]he effect of the trade practice of the company is materially increased by reason of the fact that it forms a part of the cumulative effect of the practices of the three leading companies in the tying machine industry. . . . The fact that these three companies controlled from two thirds to three fourths of the business done by the
Northern Pacific: Further Sherman-Clayton Coalescence?

Northern Pac. Ry. v. United States, the most recent Supreme Court decision dealing with restrictive contractual arrangements, although not strictly an integration case, sheds considerable light upon the possible unification of the standards of section 1 of the Sherman Act and section 3 of the Clayton Act. The railroad was charged with selling and leasing land along its right of way on condition that the buyer or lessee agree to ship his products via defendant's lines. The question presented was whether the "tie-in"—an exclusive dealing arrangement—violated section 1.

The most recent prior case dealing with the tie-in problem was Times-Picayune Publishing Co. v. United States, also a section 1 prosecution. There, the Court determined that a newspaper publisher could lawfully condition the sale of advertisements in its morning paper on the purchase of advertising in its evening newspaper. The Court based its decision on two grounds: (1) Morning and evening newspapers constitute one market rather than two; thus there was only one product sold and hence no "tie-in" existed (2) Under section 1 of the Sherman Act, a tie-in is illegal per se only if the seller enjoys a monopoly over the tying product and a significant volume of commerce in the tied product is restrained. Since there were two morning papers in New Orleans, defendant had no monopoly over the tying product, and the per se violation was held not to have been made out. According to the Court, a section 3 violation would have been easier to establish: tie-ins violate the Clayton Act when either monopoly exists over the tying product or a significant volume of commerce in the tied product is restrained. Thus,

... [A] tying arrangement may be defined as an agreement by a party to sell one product but only on the condition that the buyer also purchases a different (or tied) product, or at least agrees that he will not purchase that product from any other supplier.”

Id. at 5-6.

The Court assumed, but did not decide, that the Sherman Act's substantiality test was met. Id. at 610 n.28. This would have satisfied the § 3 standard were it applicable.
Times-Picayune contemplates a considerable difference between the standards of the two acts with respect to tie-ins.

In Times-Picayune, the Justice Department relied on section 1 rather than section 3 because it doubted that newspaper advertising could be brought within the meaning of “commodity” in section 3.268 In Northern Pacific, the tying product was land and the tied product was services as a carrier—neither of which is a section 3 “commodity.”269 Nevertheless, the Court in Northern Pacific rejected as dictum the Times-Picayune prerequisite of monopoly power over the tying product for a per se violation of section 1.270 “[Tie-ins] are unreasonable in and of themselves whenever a party has sufficient economic power with respect to the tying product to appreciably restrain free competition in the market for the tied product . . . .”271

To the authors, the language “sufficient economic power . . . to appreciably restrain free competition in the market” comes close to, if it does not go beyond, the “may” of section 3. Thus, the distinction between tie-ins which violate section 1 and those which violate section 3 has been weakened or even obliterated. All significantly anticompetitive tie-ins are now declared illegal.272 Despite the use of per se language, the rule advanced in Northern Pacific is close to the general rule-of-reason test under the Sherman Act. By using the qualifying phrase beginning with “whenever” the Court held in effect that the restrictive agreements are per se illegal, provided they are actually or constructively intended to have, or in fact have, a significant anticompetitive effect. Thus, the per se language adds little to the holding: a per se test which requires a showing of actual or potential anticompetitive effect is hardly a per se rule at all.273

268. Id. at 609 n.27.
269. See 356 U.S. at 13 & n.1 (dissenting opinion).
270. 356 U.S. at 10-11.
271. Id. at 6.
272. An example of the de minimis exception is given by Justice Black, 356 U.S. at 6-7:

Of course where the seller has no control or dominance over the tying product so that it does not represent an effectual weapon to pressure buyers into taking the tied item any restraint of trade attributable to such tying arrangements would obviously be insignificant at most. As a simple example, if one of a dozen food stores in a community were to refuse to sell flour unless the buyer also took sugar it would hardly tend to restrain competition in sugar if its competitors were ready and able to sell flour by itself.

273. The problems Northern Pacific raises with regard to the role of per se in antitrust will be considered in connection with the Klor’s case, infra notes 413-35 and accompanying text.

The preceding analysis of Northern Pacific is confined to the doctrinal level. No attempt at economic analysis is essayed, nor is any opinion ventured here as to whether the case was correctly decided on its facts. To the authors, the case is interesting primarily because it undermines the authority of Times-Picayune, which was an anticoalescence case, and because it represents an important phase in the evolution of the per se doctrine.
The Scope of Section 5

As an alternative to the Sherman-Clayton route, section 5 of the Federal Trade Commission Act offers another path to coalescence. Section 5 is a particularly potent weapon of the Government against integration systems because its violation does not presuppose a contract, combination, or conspiracy. Minimally, section 5 includes all violations of the Sherman and Clayton Acts. And certain practices may be attacked as unfair methods of competition or unfair acts or practices in commerce, via the "incipiency doctrine," even before they develop into "full blown" Clayton or Sherman Act violations.276 The outer limits of section 5 are uncertain.277

In arguing MPAS, perhaps because of uncertainty whether the Court would permit aggregation of the parallel contracts in the absence of a showing of conspiracy, the Solicitor General took the position that even if there were no Sherman Act violation there was still an FTC Act violation.278 The Court did not choose to decide the case on this basis; instead it found a section 1 violation. There is a very strong intimation, however, that the scope of section 5 goes beyond the Sherman and Clayton Acts: "The 'unfair methods of competition,' which are condemned by § 5(a) of the Act, are not confined to those that were illegal at common law or that were condemned by the Sherman Act."279 The Court then went on to discuss the "incipiency" doctrine. In the authors' view, it is quite uncertain whether the quoted remark meant only to reaffirm that section 5 embraces incipient Sherman or Clayton Act violations, or rather was intended to define a new class of offenses within section 5 which, even when "full-blown," will not constitute a Sherman or Clayton Act violation but which, nevertheless, are unfair acts, practices, or methods of competition.280 Hence, it cannot be determined at the present

277. The FTC has held a wide variety of methods of competition and acts and practices in commerce, both inside and outside the antitrust area, to be unfair. See, e.g., FTC v. R. F. Keppel & Bro., 291 U.S. 304 (1934) (lottery device held unfair method of competition); FTC v. Beech-Nut Packing Co., 257 U.S. 441 (1922) (§ 5 forbids a resale price maintenance system enforced by espionage, blacklisting); 1957 FTC AN.in. REP. 73-78 (list).
278. See note 236 supra.
279. 344 U.S. at 394. For discussion of whether this is dictum or holding, see note 237 supra.
280. The case cited as authority by the Court, FTC v. R. F. Keppel & Bro., 291 U.S. 304 (1934), is a lottery case, and the offense involved could hardly ever grow to the proportion of a Sherman or Clayton Act violation, no matter how "full blown" it became.
moment whether MPAS signals the emergence of a new category of antitrust violations applicable to exclusive dealing contract cases. Since MPAS, the Government has refrained from closely pressing the Douglas statement. Section 5 must therefore remain an enigma to the student of integration until its scope is further clarified by the Court. Perhaps, it will afford still a further means for integrating the law in this area.

Section 7 and du Pont-GM

Like section 3 of the Clayton Act, the original section 7 had a very narrow scope. The sales and commodity restrictions of section 3 found their analogue in a limitation of old section 7 to stock acquisitions; asset acquisi-

Compare 344 U.S. at 400-01 (dissent). One FTC exclusive-dealing case rejects such a broadened scope for § 5. General Mills, Inc., No. 6926, FTC, July 31, 1959 (initial order), adopted without opinion, id., Sept. 19, 1959. See also Carnation Co., No. 6172, FTC, June 26, 1959 (initial order), where it is faintly suggested that § 5 may have a higher standard of proof than § 3: actual anticompetitive effect or tendency must be demonstrated. Id. at 118, 127. FTC counsel are seeking a Commission overruling of this order.


Whether the Justice Department can invoke § 5 is uncertain. Section 5 specifically empowers the FTC to suppress unfair methods of competition, and it is doubtful that the Justice Department has concurrent jurisdiction over prosecution. See Marquette Cement Mfg. Co. v. FTC, 147 F.2d 589, 593-94 (7th Cir. 1945), aff'd sub nom. FTC v. Cement Institute, 333 U.S. 683, 701 & n.11 (1948) (Supreme Court did not directly pass on Justice Department jurisdiction as did Seventh Circuit).

For symptoms of professional alarm at the potential scope of § 5, see ATT'Y GEN. NAT'L COMM. ANTITRUST REP. 148 n.78 (1955); HANDLER, ANTITRUST IN PERSPECTIVE 39-40 (1957); Handler, Recent Antitrust Developments, 9 RECORD OF N.Y.C.B.A. 171, 182 (1954); Hodson, Exclusive Dealings, in HOW TO COMPLY WITH THE ANTITRUST LAWS 140, 148 (Van Cise & Dunn ed. 1954); cf. Gordon, Walking Backward Into the Future, in id. at 45, 48. See also Rostow, Over-All Size, in id. at 311, 315; Schwartz, Control of Affiliates, in id. at 234, 242.


tions were immune.\textsuperscript{284} And stock purchases were not severely affected since actual competition "between" the acquiring and acquired firms was usually held to be a prerequisite for the application of the act.\textsuperscript{285} This requirement, of course, rendered old section 7 inapplicable to vertical integration situations, in which the parties are not in direct competition.\textsuperscript{286} Thus, prior to 1950 section 7 was ineffective in curbing anticompetitive ownership integration.\textsuperscript{287} The shortcomings of the statute became a matter of deep concern to Congress, and consequently, in 1950, section 7 was amended\textsuperscript{288} to cover asset acquisitions and to eliminate the requirement of competition between the merging firms. The remainder of this section is devoted to a discussion of the impact of section 7 on vertical integration.\textsuperscript{289}

\textit{Section 7 Before du Pont-GM.} While no vertical integration cases arose under new section 7 before 1957,\textsuperscript{290} several horizontal merger cases were litigated during the 1950-1957 period.\textsuperscript{291} In \textit{Transamerica Corp. v. Board of Governors},\textsuperscript{292} the Third Circuit vacated a Federal Reserve Board anti-

\textsuperscript{284} This immunity was present even when asset acquisitions were the immediate consequence of a stock acquisition which itself was declared forbidden in a court action pending at the time the asset acquisition was consummated. See Arrow-Hart & Hegeman Elec. Co. v. FTC, 291 U.S. 587 (1934); Thatcher Mfg. Co. v. FTC, 272 U.S. 554, 561 (1926).

\textsuperscript{285} \textit{E.g.}, International Shoe Co. v. FTC, 280 U.S. 291, 298 (1930); V. Vivadou v. FTC, 54 F.2d 273, 276 (2d Cir. 1931); Temple Anthracite Coal Co. v. FTC, 51 F.2d 656 (3d Cir. 1931); United States v. Republic Steel Corp., 11 F. Supp. 117, 123 (N.D. Ohio 1935).


\textsuperscript{287} As a result, the more general prohibitions of the Sherman Act were utilized against vertical integration. Compare note 223 supra. The authors do not propose to review the pre-1950 history of ownership vertical integration since this subject has received excellent coverage elsewhere in the legal and economic literature. See, \textit{e.g.}, Adelman, \textit{Integration and Antitrust Policy}, 63 HARV. L. REV. 27 (1949); Bork, \textit{supra} note 284. See also Rostow, \textit{Monopoly Under the Sherman Act: Power or Purpose?}, 43 ILL. L. REV. 745 (1949).


\textsuperscript{289} Discussion of Sherman Act §§ 1-2 in the ownership integration context is omitted because new § 7 appears to cover the field. \textit{Query}: Does the term "asset acquisition" cover internal growth? Are vertical joint-venture agreements included in new § 7?

\textsuperscript{290} For a penetrating analysis of the role of § 2, see Rostow, \textit{supra} note 287.

\textsuperscript{291} Between 1950 and 1957, there were also no important Sherman Act ownership vertical integration decisions in Government cases.

\textsuperscript{292} 206 F.2d 163 (3d Cir.), \textit{cert. denied}, 346 U.S. 901 (1953) (case decided on pre-1950 § 7, but the relevant provisions of the statute were the same).
merger order, because the Board had misapplied the relevant market test. The court added, by way of dictum, that the quantitative substantiability theory of Standard Stations which the Board had used was inapplicable to section 7 situations. 293 Transamerica was enthusiastically seconded by the FTC in its interlocutory opinion in Pillsbury Mills, Inc. 294 The initial hearing examiner's dismissal of a complaint against a horizontal merger was reversed by the Commission and the remand was accompanied by a detailed discussion of the evidence to be weighed in section 7 cases. 295 The rule of Standard Stations

293 The court declared that the § 3 and § 7 rules should not be assimilated because of important differences between the two situations:
The use of exclusive dealing contracts per se lessens competition . . . so that the fact of lessening need not be proved. For one who agrees to purchase all his requirements from a single seller . . . is consequently eliminated entirely from the competitive market. In order to establish a substantial lessening of competition in such a case, therefore, it is only necessary in addition to prove that the sales covered . . . amount to a substantial portion of the total involved . . . [But] acquisition . . . is not per se a violation of the section. On the contrary such acquisition is a violation only if its effect may be in fact to substantially lessen competition between such corporations. . . . Evidence of mere size and participation in a substantial share of the line of business involved, the “quantitative substantiability” theory relied on by the Board, is not enough. 206 F.2d at 170.

The distinction advanced by this court does not seem logical. Merger eliminates competition as entirely and as “per se” as does exclusive dealing, perhaps even more so because of the greater permanence of the tie. Hence, if the court is correct in stating that it is necessary only to prove that the sales covered are substantial to establish a substantial lessening of competition in the contract case, then it should follow that no more should be necessary in a merger situation. Even though we might expect to find some valid factual distinctions between the effect of the vertical integration in Standard Stations and the horizontal or conglomerate integration, see Adelman, Acquire the Whole or Any Part of the Stock or Assets of Another Corporation, in An Antitrust Handbook 195, 204-05 (American Bar Ass'n ed. 1958), in Transamerica, the statement of the court relies on no such distinction; on the contrary, the court addresses itself only to the legal form of integration adopted.

294 50 F.T.C. 555 (1953). This merger was subsequently forbidden. Pillsbury Co., 3 Trade Reg. Rep. ¶ 27845 (FTC March 11, 1959) (initial order).

295 Pillsbury Mills, Inc., 50 F.T.C. 555 (1953). Analysis was to begin with the competitive pattern of the industry as a guide to measure the competitive effect of further concentration. Id. at 571-72. However, that an acquiring and acquired firm together control a substantial share of the market was not—as counsel supporting the complaint had asserted—an adequate index of substantial lessening of competition. Id. at 564 & n.29. The FTC cannot be deprived of the right, despite Standard Stations, to examine relevant economic factors (even in § 3 cases) when it desires to do so. Ibid. And at any rate, the § 3 standard for “substantially lessen competition” is not the § 7 standard, despite the use by Congress of the same language in both places. Id. at 562-63, 564. The appropriate standard is not specified, but its location is somewhere in the territory between the Sherman Act § 1 per se and § 1 rule of reason cases. Id. at 569. A suggestion was made that while the § 3 standard is in terms of effect on third party competitors, that of § 7 is in terms of competition. Id. at 563. The Commission conceded that the hearing examiner was being furnished “far from specific standards,” but regarded this as desirable and consistent with the “convenient
was expressly rejected. Thus, on the eve of du Pont-GM, the meager body of case law which had accumulated under new section 7\superno*\n seemed to indicate that coalescence with section 3 was unlikely. None of the cases, however, had dealt with vertical integration situations.

The du Pont-GM Case. On a literal reading, du Pont\textsuperscript{297} does not interpret the key phrase “substantially lessen competition.” The Justice Department brought suit under unamended section 7,\textsuperscript{298} which contained the “between”

vagueness” needed in antitrust proceedings, \textit{id.} at 569, and at any rate the FTC felt itself possessed of sufficient economic expertise for a case-by-case approach to the problem, \textit{id.} at 562. With the exception of the suggestion that § 7 looks to competition rather than merely to competitors—a view which the FTC might appropriately adopt in § 3 cases also, see text at notes 200-24 supra—the authors are not in sympathy with the position taken by the FTC in the Pillsbury case. In particular, they agree with the position taken in Bowman, \textit{Incipiency, Mergers and the Size Question}, \textit{1 Antitrust Bull.} 533, 537 (1956), that a case-by-case analysis, pushed far enough, is no analysis at all. See also \textit{Jewkes, Odeal by Planning} 14 (1948).

296. In addition to the cases discussed, the FTC had adopted an initial hearing examiner’s order based on what the examiner had called the “quantitative view.” A horizontal merger had united magazines controlling 20% and 15% of the relevant market; involved was nearly $20 million worth of annual business, termed “hardly . . . insignificant or unsubstantial.” \textit{Farm Journal, Inc., Trade Reg. Rep.} (1956-1957 FTC Cas.) ¶¶ 26023, 26127 (1956). The “hardly insignificant” echoes the “frugal” standard of \textit{International Salt Co. v. United States}, 332 U.S. 392, 396 (1947), deplored by the antitrust bar. \textit{Handler, Antitrust in Perspective} 36-37 (1957); \textit{Att’y Gen. Nat’l Comm. Antitrust Rep.} 147-49 (1955). See also literature cited in \textit{Handler, op. cit. supra} at 136-37, 143. The opinion also referred to possible injuries to respondent’s competitors which may be occasioned by respondents’ lower prices made possible because of economies of scale. Compare the subsequent Brillo \textit{Mfg. Co., Trade Reg. Rep.} (1957-1958 FTC Cas.) ¶ 27243 (1958), where Commission counsel’s attack on economies in production was rejected.

In another case a district court had refused a preliminary injunction requested by the Government against a horizontal merger. The Department of Justice relied solely on a comparison of sales and production figures for the acquired, acquiring, and combined firms versus the market totals. However, the court directed that the merger be so made that assets be not commingled, pending plenary action. \textit{United States v. Brown Shoe Co.}, 1956 Trade Cas. 71109 (E.D. Mo.); 24 U.S.L. Week 2369 (1956).

And in a private action brought by a watch company to prevent acquisition attempts by a competitor, \textit{Hamilton Watch Co. v. Benrus Watch Co.}, 114 F. Supp. 307 (D. Conn.), aff’d, 206 F.2d 738 (2d Cir. 1953), the court had granted a preliminary injunction under what appears to be the standard later used in \textit{Anchor Serum, supra note 200. Also of interest from this period is the private damages case, \textit{Fargo Glass & Paint Co. v. Globe Am. Corp.}, 201 F.2d 534 (7th Cir.), \textit{cert. denied}, 345 U.S. 942 (1953), brought under old § 7 and §§ 1-2 of the Sherman Act. A stove distributor sued his supplier and the firm which had bought 40% of the stock in the supplier in order to secure an output contract. The court held that the relevant market share, 25%, was far too insignificant a foreclosure to permit a finding of antitrust violation. The remaining decrees which were entered concerned purely procedural matters or were entered by consent. See \textit{Handler, Antitrust in Perspective} 136 n.6 (procedural), 135 n.3 (consent decrees and orders) (1957).


298. \textit{Id.} at 588 & n.4. The complaint also charged violation of §§ 1, 2 of the Sherman Act. The latter counts were “the focal point of eight years of litigation” and the briefs in the case. \textit{Id.} at 609 (dissenting opinion).
requirement. Since du Pont’s offense was the use of its stock interest in General Motors to secure that company’s business in fabrics and finishes, there could be no “lessening of competition” between the two corporations. Instead, the Government charged, and the Court held, that du Pont’s acquisition of twenty-three per cent of General Motor’s stock would “tend to create a monopoly.”

But in stating that “the threatened monopoly must be one which will substantially lessen competition,” the Supreme Court construed the two phrases —“substantially lessen competition” and “tend to create a monopoly”—as virtually synonymous. Hence, despite the wording of the statute, the Court explored the meaning of “substantially lessen competition” in a section 7-vertical integration context. Mr. Justice Brennan, writing for the majority, declared that the substantial lessening of competition necessary for a section 7 violation occurs when the market affected is substantial and when there is a “likelihood that competition may be ‘foreclosed in a substantial share’ of that market.” The Court noted that this is the criterion of Standard Stations.

This test, the Court found was met by GM and du Pont: GM accounted for half the automobile sales market; its automotive finish and fabric purchases must therefore have represented half those markets. Since du Pont supplied “the largest part” of GM’s requirements, with respect both to percentage and to absolute quantity, the court “must conclude that du Pont has a substantial share of the relevant market.” Thus the Court found that there was sufficient market foreclosure to allow the inference of injury to competition.

In du Pont, the Court defined the relevant market as automobile finishes and fabrics, because in its view these products “have sufficient peculiar characteristics and uses” to make them distinguishable “from all other finishes and fabrics.” But the dissent points out that these same finishes and fabrics are used in large volume by many industries other than automobile manu-

299. On appeal to the Supreme Court, the Justice Department presented as its § 7 question: “Whether DuPont’s acquisition of General Motors’ stock violates the provisions of Section 7 of the Clayton Act forbidding stock acquisitions which may result in restraint of commerce or tend to create a monopoly.” Brief for Appellant, p. 2. Again, in the main portion of its brief, the contention was made that in neither of the two clauses was there a limitation that there be competition between purchaser and the corporation whose stock is purchased. Id. at 146.

300. 353 U.S. at 590-91.

301. See id. at 593.

302. Id. at 595 & n.15; cf. id. at 593. But see id. at 607 (“reasonable probability” Query: Is this closer to the language of the test of the Jackson dissent in Standard Stations or the “not farfetched” of the majority?).

303. Id. at 596.

304. Ibid.

In 1946 du Pont sold GM 67% of its requirements for finishes; in 1947, 68% for $19 million. In 1946 du Pont sold GM 52% of its fabrics requirements; in 1947, 38% for $3.7 million. Total 1947 du Pont-GM sales were $27 million. Ibid.

305. Id. at 593-94.
facturing. For the purpose of foreclosing competitors from the market in order to effect barriers to competition, the relevant market would appear to be the entire market for the product. Economies of scale—in manufacturing, at least—depend on total output; therefore, only foreclosure from a market sufficient to prevent competitors from securing an efficient output level will bar their entry. Since the automobile market foreclosed represents only a small portion of the paint and fabric market, it would appear farfetched to infer likelihood of injury to competition in finishes and fabrics from its foreclosure.

The du Pont case is perhaps less interesting to the student of vertical integration than to the student of political science in general. The authors believe that du Pont-GM is sui generis: it involves control of the largest corporation in the country by another industrial giant. Perhaps the concentration of national economic and political power effected by this combination is more the reason for the decision than any potential anticompetitive effect on the paint and fabric industries. The authors therefore ascribe a broader policy basis for the holding than "lessening of competition" in a line of commerce. Du Pont is therefore less interesting for its result than for what it says. On the doctrinal level it appears clear that the Court rejected earlier lower court and Commission attempts to introduce an antithesis between the proscriptions of section 3 for contract integration and section 7 for ownership integration. Moreover, the decision indicates that similar considerations

306. Id. at 649-54.
307. As of 1957, GM ranked first in terms of net profits while du Pont ranked fourth. In terms of sales, GM was first while du Pont was fifteenth; for assets, GM was second, du Pont seventh. The Fortune Directory 2 (1958).

   In [the] final analysis, size in steel is the measure of the power of a handful of men over our economy. That power can be utilized with lightning speed. It can be benign or it can be dangerous. The philosophy of the Sherman Act is that it should not exist. For all power tends to develop into a government in itself. Power that controls the economy should be in the hands of elected representatives of the people, not in the hands of an industrial oligarchy. Industrial power should be decentralized. It should be scattered into many hands so that the fortunes of the people will not be dependent on the whim or caprice, the political prejudices, the emotional stability of a few self-appointed men. The fact that they are not vicious men but respectable and social minded is irrelevant. That is the philosophy and the command of the Sherman Act. It is founded on a theory of hostility to the concentration in private hands so great that only a government of the people should have it.

See also Fashion Originators Guild of America v. FTC, 312 U.S. 457, 465-66 (1941) ("the combination is ... an extra-governmental agency ... and provides extra-judicial tribunals for determination and punishment of violators, and thus 'trenches upon the power of the national legislature,' [Addyston Pipe & Steel Co. v. United States, 175 U.S. 211, 242 (1899)""); McGovern, The Power and the Glory, 46 Geo. L.J. 635 (1958).

No attempt is made here to give exhaustive analysis of the many-faceted du Pont case.
309. Although ownership ("tight-knit" combination) was subjected to a stricter "quantitative substantiality" test in du Pont than contract ("loose-knit" combination) was.
govern in individual foreclosure and collective foreclosure cases. *Du Pont-GM*, like *MPAS*, by adhering, in name at least, to the rule of *Standard Stations*, shows that the centripetal tendencies in antitrust may yet prevail over the centrifugal tendencies.

**Post-du Pont-GM Cases.** Since *du Pont*, both the courts and the Commission have had opportunity to reexamine the role of section 7 in vertical integration cases. In *Crown Zellerbach Corp.*, a dominant paper manufacturer was forbidden to engross any more of the industry. The vertical integration aspect of the case, which was not the principal issue involved, arose because a paper manufacturing firm Crown acquired had previously sold its output to independent paper jobbers and converters. Since Crown already had its own jobber and converter divisions, these independents were forced to seek a new source of supply or else buy from their competitor Crown. It is unclear from the Commission's brief discussion whether the vice seen in this particular acquisition was a potential “squeeze” of the independents by Crown, or the erection of further barriers to entry in an already concentrated industry. Perhaps, the case can best be rationalized in terms of the possibility that Crown’s acquisition would erect serious capital barriers to competition in the paper industry by making it necessary for a prospective entrant to go into the market as an integrated firm. This necessity would exist if intermediate markets became much thinner as a consequence of Crown’s horizontal integration. However, the opinion is devoid of evidence from which the existence of such barriers can be inferred.

In *Scott Paper Co.*, the Commission moved under section 7 to bar the acquisition of three suppliers by a leading paper manufacturer—the “number one company” in the sanitary paper industry. Finding a “vast difference between leadership and dominance,” the initial hearing examiner dismissed the complaint at the close of the Government’s presentation of its case. The examiner declared that Scott possessed “no control over raw materials, production, price, channels of distribution, or entry of new competitors into the market.” On appeal to the Commissioners, the dismissal was reversed and remanded for further hearings. The Commission noted that market

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311. The principal issue was the horizontal integration by Crown of half the market, almost a § 2 problem.
313. Sanitary paper includes toilet tissue, facial tissue, paper napkins, paper towels, and household waxed paper.
314. *Id.* at 36675.
316. *Id.* ¶ 27716 (Jan. 5, 1959).
concentration in the industry was high; two-thirds of the business was done by the four largest companies. "The inference is that the probability of the entry of any substantial new competitors is remote. The high cost of breaking into the market with a new product and the problems of opening channels of distribution contribute to this difficulty of entry." The FTC also considered the effect of the acquisition on competitors of Scott who relied on the acquired firms as a source of supply. These problems raised by the mergers were too grave and the record developed too insufficient to allow the case to be disposed of by motion to dismiss, and consequently the Commission remanded the case for plenary action.

The third post-du Pont Commission order involved the acquisition of a converter of plain aluminum foil into decorative aluminum foil by its supplier, the Reynolds Metal Company. The relevant market was defined as decorative aluminum foil, rather than all aluminum foil or all aluminum, because of the unique characteristics of decorative foil. In this market, the acquired firm accounted for twenty-five per cent of sales volume. The examiner found as a fact that Reynolds acquired, by the merger, "the power to exclude its aluminum foil producing competitors from selling to [the acquired firm, whose purchases were] ... quite important sales-wise not only to respondent but to its competitors, Alcoa, Kaiser and others. ..." Alleged foreclosure of these competitors from the market was not, however, the basis of the initial examiner's order. The market in which the likelihood of substantially lessening competition was found was the converted decorative foil market. Before expansion by Reynolds, entry into foil conversion had "been easy, with low capital outlay, standardized and plentiful machinery, no dearth of supplies." But Reynolds' arrival on the scene was found to have "materially altered this picture," by putting a firm with 600 million dollars in assets into competition with the eight or ten small converters who specialized in decorative foil. Reynolds had economic power to wage fierce and predatory competition with the established converters solely because of its deep pockets. Moreover, because of its wide conglomerate of activities, Reynolds could secure horizontal economies of scale, for example, in styling and advertising, which were unavailable to its competitors. The result was asserted to be that "the low cost, ease of entry, plentiful supply of basic material and ..."
machinery while still there, are, in effect, unusable.\textsuperscript{326} To the argument that the merger had negligible effects on competition itself, the examiner retorted that this argument seems to be founded basically on the assumption that the law ignores the capture of small markets from small businessmen. This hearing examiner does not believe the statute as amended was so intended. This case presents the picture of eight or ten small commercial units in imminent danger of being forced out of a formerly commercially livable enterprise by reason of the acquisition attacked. . . . If the present and probable plight of these victims is to be ignored and written off as too insignificant, it will have to be for others, at higher levels, to do it.\textsuperscript{327}

Whether the “plight of these victims” should be ignored and written off is a subject to which this study will return later. At this point, it is sufficient to observe that Reynolds appears to have been condemned primarily for its efficiency.\textsuperscript{328} The objection that Reynolds had power to wage predatory competition, because of its “deep pockets,” would appear relevant whenever a wealthy corporation, or even an entrepreneur with a rich aunt, acquires a firm or starts a business. At most this is a size problem, rather than a vertical integration problem.

Similar solicitude for the plight of the customer in competition with his supplier is shown in United States v. Bethlehem Steel Corp.\textsuperscript{329} As in the Crown case,\textsuperscript{330} the proposed integration was primarily horizontal.\textsuperscript{331} But there were small, independent fabricators of steel, who bought from and sold to Youngstown, one of the two merging firms, various fabricated or semifabricated steel products. For example, Youngstown accounted for over ten per cent of the wire for wire rope produced by nonintegrated manufacturers.\textsuperscript{332} The other integrating firm, Bethlehem, had its own divisions in these fields. “In view of the price squeeze and other competitive disadvantages under which the independent wire rope fabricators labor, to remove Youngstown as a source of supply would render even more hazardous the competitive position of the independents, and might well mean the difference between their continued existence and their extinction.”\textsuperscript{333} Moreover, Youngstown purchased 1.3 per cent of all wire rope manufactured in the country, and in some cases as much as ten per cent of an independent fabricator’s output. Since, as a result of the

\textsuperscript{326} Ibid. (finding 64).
\textsuperscript{327} Id. at 25.
\textsuperscript{328} Compare Adelman, Integration and Antitrust Policy, 63 Harv. L. Rev. 27, 52-53 (1949).
\textsuperscript{330} See text at note 310 supra.
\textsuperscript{331} 168 F. Supp. at 611.
\textsuperscript{332} The court considered the relevant market to be wire produced by firms not competing in the manufacture and sale of fabricated wire rope, because firms integrated forward into rope fabrication represent a precarious source of supply to the independent. Id. at 612-13. The precariousness results principally from actual or potential price squeezes. Ibid.; see text at note 333.
\textsuperscript{333} 168 F. Supp. at 613.
merger, Youngstown's needs would presumably be supplied by the Bethlehem wire rope fabrication division, the court concluded:

The impact [of the merger] would be . . . a significant restriction of access to a vital source of supply and also to a needed market. Thus the merger presents a double-edged threat to the independent wire rope fabricators. Here it may be emphasized that one of the factors which led to the passage of section 7 was threat to small business by the merger movement. The proposed merger poses just that threat.\textsuperscript{334}

The merger was enjoined as violative of section 7. The decision is based primarily on the horizontal integration issues, however, and we can only conjecture how the court would have treated the vertical aspect of the case had it stood alone.

The recent case of \textit{United States v. Maryland & Va. Milk Producers Ass'n} \textsuperscript{335} is the only vertical integration decision under new section 7 presenting an unambiguous "leverage" problem, \textit{i.e.}, the use of power at one level—distribution—to secure or strengthen power at another level—production.\textsuperscript{336} The defendant milk association is an agricultural cooperative of about 2000 dairy farmers in Maryland and Virginia. About eighty-six per cent of milk sales to dealers in the District of Columbia area—one relevant market—were made by this co-op. Another ten per cent of area sales were accounted for by "a disturbing influence which [had] been a thorn in the side of the Association for many years"\textsuperscript{337}—the Embassy Dairy. In the second relevant market—sales made to Governmental installations in the area—the co-op accounted for forty-five per cent of total volume while Embassy sold forty-seven per cent.\textsuperscript{338} Embassy bought its raw milk from about 120 independent farmers (so-called "bootleggers") who did not belong to the co-op and whose product was characterized as "distress milk."\textsuperscript{339} Embassy, through its ability to buy cheap milk from independents, had cut heavily into co-op sales. Between loss of sales and Embassy price pressure, co-op producers lost revenues of 700,000 dollars a year.\textsuperscript{340} The defendant's solution to its problem was to buy Embassy out.\textsuperscript{341}

\textsuperscript{334} \textit{Ibid.}


\textsuperscript{336} For the reasons given in text at notes 309-11 \textit{supra} the authors do not consider \textit{du Pont} to present an unambiguous leverage problem.

\textsuperscript{337} 167 F. Supp. at 804-05. The quotation comes from an internal memorandum of the association written by its general manager.

\textsuperscript{338} The size of the Government market, about $2 million a year, is quite "minor in proportion" to the total market, 167 F. Supp. at 804, amounting to about 7%-10% of the latter, see \textit{id.} at 804-05 (authors' computation); Record on Appeal, p. 557 (§1-$2 million estimate).

\textsuperscript{339} See 167 F. Supp. at 805. Embassy secured about three-quarters of its supply from local independent producers and the balance from others, including middlemen. Record on Appeal, p. 647.

\textsuperscript{340} See 167 F. Supp. at 805-06. Embassy, although a low volume producer, was able to act as an area price leader. See \textit{Boulding, Economic Analysis} 644-45 (3d ed. 1955).

\textsuperscript{341} In setting its sale price, Embassy exacted from the co-op the value of the mo-
The result of the merger, at least for the time being, was to eliminate the "distress milk" from the market. The independent producers no longer had access to the Washington market unless they would join the co-op. Some of them chose to do this, but most stopped shipping their output to the District market and began shipping, instead, to Baltimore. Embassy's price pressure on the Government and consumer markets ceased. Thus, by vertical integration, the co-op removed its competitors' means of distribution, thereby foreclosing them from the market and securing to itself a monopoly of production. For

342. Id. at 806.

343. The foreclosure of the market thus realized, however, was not complete. "Apparently the continued existence of several comparatively small dairies kept alive considerable competition in the industry." Ibid. The former role of Embassy is now, to a large extent, played by High's Dairy, a vigorous and aggressive competitor who relies on independents for supply. See Record on Appeal, pp. 632, 634.

344. The market situation may be represented, in greatly simplified form, diagrammatically as follows:

### Before Merger

**Production**

- 2000 Co-op Dairy Farmers
- 120 Independent Dairy farmers

**Wholesaling**

- Dairies Buying From Co-op
- Embassy

**Retail**

- 86% of Sales in D.C. plus 45% of Federal Sales
- 10% of Sales in D.C. plus 47% of Federal Sales
- Baltimore

### After Merger

**Production**

- Co-op Dairy Farmers
- Independent Dairy Farmers

**Wholesaling**

- Dairies Buying From Co-op plus Embassy

**Retail**

- 95% of Sales in D.C. plus 92% of Federal Sales
- Baltimore
VERTICAL INTEGRATION

this strategy to work, it would be necessary that entry into wholesale distribution be difficult. Otherwise, a new competitor could step in and threaten the expensively purchased monopoly. Apparently, there was some degree of imperfection in the market or barriers to entry into milk wholesaling, because the court found that the strategy was successful. But the opinion is utterly silent on the nature of the barriers.\textsuperscript{345}

\textit{The Future of Section 7.} The full scope of new section 7 has not yet been defined, but the courts may soon probe its frontiers. Until 1958, action had been taken only against acquisitions of entire enterprises by another. Asset acquisitions within section 7 are, however, expressly not limited to the merger of firms.\textsuperscript{346} The legislative history of the Celler-Kefauver Act is vague on the point of what constitutes an asset acquisition. The most pertinent discussion touching the question is in the House Report: “It [the bill] covers not only the purchase of assets or stock but also any other method of acquisition, such as, for example, lease of assets. It forbids not only direct acquisitions but also indirect acquisitions, whether through a subsidiary or affiliate or otherwise.”\textsuperscript{347}

Moreover, the term “asset” may not be restricted to tangible property; intangibles or choses in action may be included as well.\textsuperscript{348} In the Senate hearings on the bill, a manufacturers’ association suggested an amendment defining “[a]ssets . . . not [to] include stock in trade, inventories, or other property held by a corporation primarily for sale in the ordinary course of business.”

\textsuperscript{345} Perhaps, when the percentage of market control goes above 90\%, courts are entitled to use a conclusive presumption of foreclosure without singling out any particular barrier to entry. This appears to be the rationale of Judge Learned Hand’s celebrated dictum in United States v. Aluminum Co. of America, 148 F.2d 416, 424 (2d Cir. 1945), that 90\% control of the market “is enough to constitute a monopoly; [but] it is doubtful whether sixty or sixty-four percent would be enough, and certainly thirty-three percent is not.” If the presumption is valid in the context of § 2, which is the most difficult antitrust statute for the prosecutor to prove violated, a fortiori the presumption is valid for a “may” statute like § 7.

Even § 2, however, permits the defense to prove that monopoly was “thrust upon” it. \textit{Id.} at 429-31; United States v. United Shoe Mach. Corp., 110 F. Supp. 295, 342 (D. Mass. 1953), \textit{aff’d per curiam}, 347 U.S. 521 (1954). But, as we have seen, § 3 of the Clayton Act allows no affirmative defenses at all, see text at notes 104-08 \textit{supra}, while the only affirmative defense which has consistently prevailed under § 7 is that of the “failing competitor,” see Comment, 68 \textit{Yale L.J.} 1627, 1662-68 (1959). Perhaps in the absence of availability of affirmative defenses, adoption of a conclusive presumption of anticompetitive effect, despite lack of showing by plaintiff of potential barriers to entry, is unduly harsh on defendants.


\textsuperscript{347} H.R. \textit{Rep.} No. 1191, 81st Cong., 1st Sess. 8-9 (1949).

\textsuperscript{348} The only chose in action covered expressly by § 7 is stock. \textit{Ibid.}; see Farm Journal, Inc., \textit{Trade Reg. Rep.} (1956-1957 FTC Cas.) ¶ 26023 (1956) (initial order), \textit{adopted without appeal}, id. ¶ 26127 (Commission cease and desist order).

The legislative history of the 1950 amendment to Section 7 of the Clayton Act, the amendment itself, and its purpose, persuade the hearing examiner that the term ‘assets’ as used therein means property or property rights, real or personal, tangible
ness." No action was taken on the proposal. This may indicate congressional determination to leave the concept of "asset" broad and flexible, or it may equally well manifest lack of congressional appreciation that "asset" is not a fully determinate concept without troublesome ramifications.

Two recent Justice Department complaints raise interesting problems in the interpretation of this portion of the statute. When Universal Pictures conveyed the exclusive television rights to its library of pre-1948 films to Screen Gems, a distributing subsidiary of Columbia Pictures, the Government brought an action charging violations of section 1 of the Sherman Act and section 7 of the Clayton Act. The transaction may fit more easily into the conceptual pigeonhole of "asset transfer" when it is labelled a sale of an "exclusive license," as the complaint does. But this license is extremely close to an output contract. By pleading under Clayton Act section 7, in such cases, the "easier"

or intangible which is subject to transfer and which has been used by the seller and could be used by the buyer competitively.

Quoted in 1 TRADE REG. REP. 4205.200 (10th ed.). The foregoing refers to an acquisition of a subscription list and the "right to solicit" subscriptions from those on the list.

In Bender v. Hearst Corp., 152 F. Supp. 569, 578-79 (D. Conn. 1957), an advance sheet service which supplied information on estimated parts and labor costs for various car repairs was acquired by a competitor. The assets consisted of trade names, copyrights, technical data, records and forms, and goodwill. The court held the assets in question were not subject to § 7, because they were the property of an individual rather than a corporation, as § 7 requires. However, the court went on to say that "except for this, it is apparent" that § 7 would apply. In affirming, the Second Circuit held § 7 inapplicable because there was no proof of "public injury," and thus did not address itself to the question of whether the assets in question came within the asset definition of § 7.


351. Compare Complaint, p. 7 ("defendant Screen Gems acquired assets of defendant Universal, said assets consisting of an exclusive license . . . for exhibition . . . [of] defendant Universal's library of . . . films") (§ 7 count), with id. at 6 ("defendants have effectuated the aforesaid combination and conspiracy in part by means of a contract . . . [for] the exclusive license to distribute . . .") (§ 1 count).

In *Screen Gems*, defendants first contended that § 7 covers only "physical" assets. Defendant's Memorandum Submitted in Opposition to Plaintiff's Motion for Summary Judgment and Preliminary Injunction, pp. 49-50. They subsequently shifted their position and now deny "acquisition" of assets. Their theory is that "acquire" refers to "title" or "ownership" and that this transaction falls far short of conveying either of these. Defendant's Memorandum Regarding the Meaning of "Assets." Defendants reaffirmed their position that they did not "acquire" assets in their Memorandum for Pretrial Conference.

352. Of course an output contract is usually for entire future output, i.e., for future goods, while the Columbia-Universal license covered an entire past output, i.e., specific goods. Query: Are Sales Act distinctions helpful here?
Clayton Act standard may be invoked despite the restrictive wording of section 3 of that statute. 353

When Monsanto conveyed to Lever Brothers all its rights in the synthetic detergent "all," and Lever agreed to buy from Monsanto its requirements of the ingredients of "all," 354 the Justice Department filed a complaint praying that "the contractual arrangement between Lever and Monsanto and the resulting acquisitions . . . be adjudged in violation of Section 7 of the Clayton Act" and that "Lever be required to divest itself of the . . . rights acquired . . . under the contractual arrangement." 355 As in the Columbia Pictures license transfer, the contractual arrangement has "asset" overtones. Trademarks, copyrights, and patents related to "all" were transferred. Thus, the case is not purely one of a requirements contract. Moreover, despite the joinder of Monsanto as a co-defendant, the action and the relief requested are directed primarily against the buyer Lever, 356 who is the party bound by the restrictive arrangement. 357

353. See note 225 supra. A more recent complaint in the television industry deals with an even greater fragmentation of the bundle of rights involved in motion picture copyrights. One asset acquisition attacked in Complaint, United States v. United Artists Corp., Civ. No. 150-267, S.D.N.Y., Sept. 15, 1959, TRADE REG. REP. ¶ 4059, at 66404 (case 1477) (summary of complaint), is that of "residual rights" after the preliminary exhibition of a film library. Such rights are analogous to the reversionary interest of a fee holder after the grant of a term of years. Hence, the rights have not only been divided according to the field of exploitation, but also along the plane of time.

The Columbia Pictures case does not appear to represent a case of barriers to entry caused by vertical integration. The complaint appears to have strong overtones of purely horizontal combination reminiscent of the early railroad cases: United States v. Southern Pac. R.R., 259 U.S. 214 (1922); United States v. Union Pac. R.R., 226 U.S. 61 (1912); Northern Sec. Co. v. United States, 193 U.S. 197 (1904); United States v. Joint Traffic Ass'n, 171 U.S. 505 (1898); cf. Swift & Co. v. United States, 196 U.S. 375 (1905). See generally Phade, Screen Gems, 8 CARTEL 123 (1958). Thus, the interest of the case to the student of vertical integration is directed primarily to the doctrinal issues involved.

354. In May, Lever Brothers Company purchased from us the trademark and franchise to market the detergent all and Dishwasher all. We have contracted to manufacture these products for Lever Brothers for a period of years and, for an interim period, to package them.

This agreement permits Monsanto, in the detergent field, to devote all of its energies to the development and sale of its chemicals to detergent manufacturers.


356. The complaint prays that the Monsanto-Lever requirements contract be adjudged in violation of § 7, but no relief against Monsanto is asked. Complaint, pp. 8-9. The court is asked to decree divesture against Lever and enjoin it from making any further acquisitions from corporations in the soap or detergent business. Ibid.

357. Lever is bound to deal exclusively with Monsanto for its "all" requirements. Of course, under this integration contract, Monsanto is bound to supply Lever with all the "all" it requires. However, there is no indication that Monsanto is bound not to sell detergent chemicals to others than Lever. Thus, in Monsanto Ann. Rep., 1957, p. 7, it is stated that the agreement will make it possible for Monsanto "to devote all of its energies to the development and sale of its chemicals to detergent manufacturers."
Nevertheless, the complaint suggests the potentiality of section 7 for neutralizing the commodities limitation of section 3.358 Thus, a contract by which the buyer agrees to purchase all its requirements of some service might be vulnerable, because the seller acquires the “asset” constituted by his contractual rights.

And there may well be further latent possibilities in the asset clause of section 7, since there is nothing in the statute to limit its application to the exclusive dealing context. Any contract creates mutual rights in the parties which have many of the incidents normally associated with assets, such as real or personal property: most contractual rights can be sold, assigned, or hypothecated.359 When the acquisition of contract rights tends substantially to lessen competition, there may be a section 7 problem. Impatience or dissatisfaction with imagined difficulties of proof under the Sherman Act rule of reason or resurgence of a trend against Sherman-Clayton coalescence could motivate attempts to expand the concept of “assets” under revised section 7.360

Conclusion

Three routes by which the courts do or may unify the law of vertical integration have been explored. One possible route is over-all coalescence of the standards of the Clayton Act and section 1 of the Sherman Act. A second route exists via section 5 of the Federal Trade Commission Act, but this is a route which only the Commission can take and on which the Department of Justice and private litigants cannot travel. Expansion of section 7 of the Clayton Act to cover contractual arrangements offers a third possibility, but any conclusions about its role would be premature.

In any case, further unification of the law in this area is to be anticipated. Still, the distinction between industrial integration by ownership and by contract retains its value. Contract integration is more impermanent and reversible a tie than is ownership. For that reason, perhaps a greater degree of integration is tolerable when contract is used. Perhaps, also, there exist valid functional distinctions between forward and backward vertical integration, and the extent to which integration may proceed before anticompetitive effects are felt may differ with the direction. But compartmentalization of the law of integration into a section 1 test for backward integration by contract, a section 3 test for forward integration by contract, and a section 7 test for ownership integration is not rational, unless these heterogeneous standards are based on

358. The thrust of the Government’s complaint is against Lever, the requirements contract purchaser. See note 356 supra. Use of § 3, which is directed against requirements contract sellers, “would probably not lead to satisfactory relief.
359. See 4 CORBIN, CONTRACTS § 860 (1951).
360. Compare the efforts to expand the per se rule against vertical integration. Compare United States v. Yellow Cab Co., 332 U.S. 218 (1947), with United States v. Paramount Pictures, Inc., 334 U.S. 131, 173-74 (1948), and United States v. Columbia Steel Co., 334 U.S. 495, 521 & n.18, 523-25 (1948). While we cannot predict how far § 7 will take the courts, it appears safe to say that refusals to deal are beyond its scope, since a refusal to deal could hardly be considered a direct or indirect “asset acquisition.”
the differing economic impact of the various forms of integration. In the cases in which the Government moved against integration systems, the courts appear to have recognized that the three statutes do not embody different standards established on such a basis. As a result, they have declined to measure the legality of the different types of vertical integration with tests based purely on formal differences in the wording of the statutes.

Although it appears that a single criterion of legality for integration systems is evolving, it is not yet clear what that standard will be. Certainly, the standard is closely linked with the term "foreclosure." But the meaning of this key word is much debated. To the authors, it is properly identified with barriers to competition itself. As they read the Supreme Court cases, this is the meaning of "substantially lessen competition" and "unreasonably restrain trade" in the key decisions. But strong indications exist that the FTC regards foreclosure as mere injury to competitors. The struggle over whether antitrust exists solely to monitor free competition in the market place, or to redress torts or private wrongs as well, is a central issue in an analysis of the law of vertical integration and one to which this study will return again.

Refusals To Deal: Private Suits and Vertical Integration by Contract

Vertical integration by contract or ownership is banned by the antitrust laws whenever it may substantially lessen competition, unreasonably restrain trade, or constitute an unfair method of competition. The ban applies to restrictive agreements irrespective of their form as express provisions or informal understandings backed up by the threat of refusal to deal. These arrangements may be dissolved by the courts at the behest of the Government, and criminal sanctions may be imposed upon the firm and its officers.361

But the Government is not the only litigant in antitrust. As a needed supplement to public enforcement of the antitrust laws, Congress has provided for private antitrust suits as well.362 Three classes of private litigants are found in vertical integration cases: (1) competitors of the integrating firm, (2) the integrated firm itself, and (3) firms subjected to the refusal to deal sanction. Relatively few cases in the first category have been brought,363 but competitors


363. Fargo Glass & Paint Co. v. Globe Am. Corp., 201 F.2d 534 (7th Cir. 1953), cert. denied, 345 U.S. 942 (1953); Oxford Varnish Corp. v. Ault & Wiborg Corp., 83 F.2d 764 (6th Cir. 1936); Pick Mfg. Co. v. General Motors Corp., 80 F.2d 641 (7th Cir. 1935),
injured by the integration system should be able to seek damages or an injunction on the same legal theories as are available to the Government.⁶⁳⁴ The few cases in the second category, between firms related by integration, have established that courts will deny the integrating firm the right to invoke legal sanctions to preserve its position if there is an antitrust violation. The disgruntled contract integrated buyer⁶⁶⁵ or seller⁶⁸⁸ may refuse to carry out his contracts with impunity, or he may even sue for and collect treble damages.⁶⁹⁷ In ownership integration situations the right to vote the stock of an acquired firm may be enjoined and damages may be levied by opposition stockholders.⁶⁶⁹ Thus, it appears that there are ample private remedies available, at least in principle, to competitors or members of an integration system.


364. But see McElhenney Co. v. Western Auto Supply Co., 167 F. Supp. 949, 954 (W.D.S.C. 1958) (dictum), aff'd and remanded, 269 F.2d 332 (4th Cir. 1959). The authors submit that there is no basis in the case law or in policy for the distinction the district court found between suits by the Government and by a competitor.


366. See Tempa Elec. Co. v. Nashville Coal Co., 168 F. Supp. 456 (M.D. Tenn. 1958). This case should be disapproved on its facts, which do not bring it within the rule of Standard Stations. The reasoning of the court seems to be an extreme example of the Anctwr Serum approach. See note 203 supra and accompanying text.


However, these potential litigants have seldom availed themselves of the antitrust laws. While an integration relationship is functioning, an integrated firm usually would be reluctant to jeopardize its position by bringing a lawsuit. The relatively speculative nature of the damages a firm sustains because of integration, and possibly the fear of a pari delicto defense may further deter such suits. For competitors of integrating firms, the evidentiary problems illustrated by *J. I. Case* probably discourage many suits.

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371. See notes 368 and 369 *supra*. However, injury to the integrated firm has figured in two important cases. In United States v. Yellow Cab Co., 332 U.S. 218 (1948), a complaint was held to state a cause of action under §§ 1-2 when an integration system was alleged to injure the public, the integrated firms, and competitors of the integrating firm:

> It is said that appellees have agreed to control the operation and purchase of taxicabs by the principal operating companies in Chicago, New York City, Pittsburgh and Minneapolis, insisting that they purchase their cabs exclusively from CCM.... [T]he trade of the controlled cab companies is restrained since they are prevented from purchasing cabs from manufacturers other than CCM. The result allegedly is that these companies must pay more for cabs than they would otherwise pay, their other expenditures are increased unnecessarily and the public is charged high rates for the transportation services rendered. ... [B]y preventing the cab operating companies under their control from purchasing cabs from manufacturers other than CCM, the appellees deny those companies the opportunity to purchase cabs in a free, competitive market.5

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5 To the extent that the controlled operating companies are charged higher than the open market prices, they are injured.

*Id.* at 224-27 & n.5. In Hamilton Watch Co. v. Benrus Watch Co., 114 F. Supp. 307 (D. Conn.), aff’d, 205 F.2d 738 (2d Cir. 1953), a preliminary injunction was granted against stock voting by a watch manufacturer who sought to take over control of one of his competitors, or at least obtain representation on its board. “[T]he immediate effect of such representation would be... as between Hamilton and Benrus to improve the competitive position of Benrus with a reciprocal impairment of Hamilton’s position.” 114 F. Supp. at 317. However, the court also found likelihood of lessening of competition between the two firms, and the question of private harm was probably important only because the action was a private suit rather than one brought by the Government. Perhaps the *du Pont-GM* case also has faint overtones of injury to the integrated firm. And there are references in *Standard Stations, Richfield*, and the reappraisal of *Standard Stations* in the *MJPS* dissent, to the effect of the integration system on the retail operators. However, no case is authority for the proposition that an antitrust violation can be predicated purely upon injury to a firm integrated into the industrial empire of another firm. *But see* Red Rock Bottlers, Inc. v. Red Rock Cola Co., 1952-1953 Trade Cas. 67962 (N.D. Ga. 1952).

372. Such fears may be quite unwarranted; “the effectiveness of In Pari Delicto as a defense has been considerably limited [in antitrust suits]...” *Banana Distrbs., Inc. v. United Fruit Co.*, 162 F. Supp. 32, 45 (S.D.N.Y. 1958) (dictum) (collecting authorities).

373. Moreover, by the time the relationship collapses, the statute of limitations may bar recovery of the greater part of the damages accrued, thus making a suit unprofitable.

374. See text at notes 173-80 *supra*. 
In contrast, the firm subjected to the refusal to deal sanction because it declines integration faces no evidentiary problem. The negotiations leading up to the refusal to deal will usually provide ample evidence that the refusal is rooted in an exclusivity policy. At the same time, the dealer who is cast out no longer has any relationship to jeopardize, and his reluctance to offend the integrating firm vanishes. But paradoxically the cast-out dealer, despite his most advantageous position to vindicate the public interest in free competition by acting as a private law enforcement agency, is the one potential litigant to whom the courts uniformly deny a remedy under the antitrust laws. Serious technical obstacles created by the wording of the statutes presently bar relief in such actions, and the cases have often been decided on the pleadings. In addition to these technical problems, the courts have been confronted in cancelled dealer cases with grave problems of public policy which touch upon the function of antitrust. The proper scope and function of the treble damages action is not settled: the clash between antitrust as tort and as the guardian of competition continues to trouble the courts.

The Cause of Action Under Section 4

Private damage suits are available to a party injured by a violation of the antitrust laws under section 4 of the Clayton Act which allows treble damage recovery to "any person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws." According to the case law, a cause of action under section 4 has three essential ingredients: (1) a violation of the antitrust laws by defendant, (2) an injury to plaintiff, and (3) a
proximate-cause relationship between the violation and plaintiff's injury. Typically, cancelled dealers have been unable to make out one or more of these ingredients.

The Nelson Case

All of these issues are raised in Nelson Radio & Supply Co. v. Motorola, Inc., the leading cancelled dealer treble damages case. Nelson, a radio equipment jobber, was cut off by his supplier, Motorola, when he refused to accede to a demand that he agree to deal on an exclusive basis. In his complaint, Nelson alleged violation of sections 1 and 3. The court dismissed the complaint for failure to state a claim on which relief could be granted—in more traditional terminology, failure to state a cause of action.

Consummated Sales and Intracorporate Conspiracy. Section 3 of the Clayton Act forbids only sales made on condition, agreement, or understanding of exclusive dealing. According to the Nelson court, a dealer who is disciplined by nonrenewal or termination, because he refuses to deal exclusively with his supplier, cannot invoke this statute because no sale at all has been made to him. Equally serious obstacles prevent recovery under section 1 of the Sherman Act. Between the cancelled dealer and the manufacturer no injurious contract, combination, or conspiracy exists of which complaint can be made. To overcome this obstacle, Nelson alleged a combination or conspiracy by Motorola and its officials of which he was the victim. The court refused to entertain the "absurd assertion"382 of a combination or conspiracy between a corporation and its officers or agents.383


379. 200 F.2d 911 (5th Cir. 1952), cert. denied, 345 U.S. 925 (1953).
380. See 200 F.2d at 913, 915.
383. Attack under Sherman Act § 2 dispenses with the conspiracy problem, but monopolization has not been successfully proved in dealership cases because of the existence,
Proximate cause. As an alternative, Nelson charged that the consummated sales Motorola made to jobbers who acceded to the demand for exclusive dealing were violations of section 3. But the court regarded these sales as causing no injury to the plaintiff: "[I]t is the absence of a contract with the plaintiff, not the presence of agreements with distributors in other parts of the country, of which the plaintiff must complain."\textsuperscript{384} It appears likely, given this view of proximate cause, that the court would have made the same response had Nelson made the section 1 argument that these sales agreements with others were contracts, combinations, or conspiracies in unreasonable restraint of trade in violation of section 1.

With the help of statutory interpretation, the Nelson court was thus able to dismiss the complaint on the pleadings. It never reached the issues of substantial lessening of competition or unreasonable restraint of trade. From the record in the Nelson case we have very little basis for deciding whether Motorola's practices had an actual or incipient anticompetitive effect. Motorola's share of the national market was greater than fifty per cent of sales volume.\textsuperscript{385} No information was given however, on Motorola's share of available jobbers, on their choice quality, on the ease of entry into the jobber-market,\textsuperscript{386} or on other relevant economic factors. Nelson was never given an opportunity to introduce such evidence. The absence of pertinent data makes it impossible to determine whether the share of the market foreclosed by Motorola had an adverse effect on competition.

Refusal To Deal and Public Policy

The Nelson decision raises grave problems of public policy. According to the interpretation of the antitrust laws adopted by the court, a refusal to deal with a dealer who has not acceded to the request for exclusivity is not actionable, even if it is a means of controlling a system of exclusive dealing which has anticompetitive effects. This is true even though the system could be challenged by the Government or by a competitor of the integrating firm. Thus, absent action by the Government (which does not have the time or resources to intervene in every anticompetitive scheme) and suit by a competitor (who may often have a similar scheme of exclusivity and therefore would not sue) customarily, of reasonably close substitutes competing with defendant's product. See, e.g., Miller Motors, Inc. v. Ford Motor Co., 252 F.2d 441 (4th Cir. 1958); Packard Motor Car Co. v. Webster Motor Car Co., 243 F.2d 418 (D.C. Cir. 1957). But see Eastman Kodak Co. v. Southern Photo Materials Co., 273 U.S. 359 (1927). No § 2 charge was involved in Nelson-Motorola. See Brief for Respondent on Petition for Certiorari, p. 5.

\textsuperscript{384} 200 F.2d at 915; accord, Simpson v. Union Oil Co., 162 F. Supp. 746 (N.D. Cal. 1958).

\textsuperscript{385} 200 F.2d at 913.

\textsuperscript{386} Motorola denied that the case presented a situation where there was no room in the market for newcomers. Entry into distribution was alleged to be free. However, no support for this position was given. See Brief for Respondent on Petition for Certiorari, pp. 12-14.
the firm wanting to integrate has a device available which exposes it to a minimum of legal risk. As a result of the Nelson doctrine, there emerges in addition to integration by ownership and integration by contract, a third category—integration by refusal to deal—which differs from ordinary contract integration only in that no integration (i.e., exclusive dealing) clause or its equivalent exists; the integration system places sole reliance on the threat of refusal to deal. This is a most effective way of protecting exclusivity; first, it replaces contract sanctions—i.e., damages, rescission, or specific performance—whose invocation would be futile anyhow. Second, it avoids the risk that exclusive dealing clauses might be used as evidence in an antitrust action. Third, for the dealers who are not admitted to the system or who are cast out because they refuse to accept integration, the Nelson case—literally interpreted—creates unsurmountable doctrinal obstacles to a claim for damages.

Consequently, Nelson deserves close examination to determine whether the decision is required by a fair reading of the law. Should this be the case, we must realize that there is a real difference between public and private antitrust law, at least in the refusal-to-deal area, which the courts must recognize, and the resolution of which must be left to Congress to deal with. An alternative solution, on the legislative level, will be proposed in a succeeding section.

It is these facets of the Nelson case which constantly should be kept in mind when reading the pages that follow, which are directed against the Nelson doctrine. To understand its full significance, let us postulate a situation where either the Government or a competitor could bring an antitrust suit because the activities of the defendant have brought about or may bring about a substantial lessening in competition. Let us postulate further, to avoid evidentiary issues, that the defendant's refusal to sell is not based on legitimate reasons, business or otherwise, but clearly on plaintiff's unwillingness to deal exclusively. Given such fact situations, is a court unable under present law to protect competition at the instance of an injured dealer because of the wording of the antitrust laws?

Section 3 and Proximate Cause

The narrow wording of the statute leaves little leeway for any other interpretation than that adopted by the courts. Even if courts would construe "sale" as used in the act to include "offer to sell," or "contract to sell" to include "offer to contract to sell," the problem of proximate cause would still prove an obstacle to use of the statute against refusal to deal. The offer to sell on condition of exclusive dealing is not itself the cause of injury. Rather the injury flows from the refusal to sell on nonexclusive terms. While "sale" could conceivably be stretched to include "offer to sell," the term is hardly so elastic as to cover "refusal to sell." As a result, the only section 3 violation in sight is

387. E.g., a minimum quantity clause like that in the Richfield case. See text at note 173 supra.

388. Compare, however, the liberties taken by the Supreme Court with "every" in § 1 of the Sherman Act. Handler, Antitrust in Perspective 3-28 (1957). This construction,
with respect to the consummated sales which are made to those buyers who agree to the proposal for exclusive dealing. The Nelson case rejected the argument that this violation caused injury to the would-be buyer who does not submit to the proposal. The counter-argument could be made that the disappointed buyer is injured by the contracts with those buyers who submit to exclusive terms because, without the consummated restrictive sales to the others, it would be impossible for the seller to exert economic pressure on dealers who try to hold out for nonexclusive terms. Thus, if the exclusive contracts with others substantially lessen competition, it could be argued that the entire integration system violates section 3. Since the system is enforced by the refusal-to-deal sanction, injury caused by refusal to deal is, arguably at least, injury "by reason of" an antitrust violation. Such an approach would get around the proximate cause problem.

Expansion of Section 1 Conspiracy

The Sherman Act which focuses attention on conspiracy in restraint of trade, offers another possibility for further doctrinal evolution in this area.

however, was restrictive rather than expansive. For an unexpected expansive interpretation, see du Pont-GM, discussed at notes 297-309 supra and accompanying text, noted in 66 YALE L.J. 1251 (1957) (old § 7 applied to vertical integration, and suit 30 years after acquisition).

389. See text at note 384 supra.

390. Such a theory is based on the supposition that submission to exclusivity by n-1 dealers exerts a coercive pressure on the nth dealer. That is, but for submission by the n-1 dealers, the nth dealer could successfully resist. Query: Is this indeed the case? Is there any economic "leverage" exerted this way? Perhaps, when dealers in California, Texas, New York and Ohio all agree to contracts in violation of § 3, this gives Motorola the knowledge that it can succeed in imposing restrictive contracts on dealers. Such knowledge adds to Motorola's power, in effect, and thus makes it more feasible for Motorola to demand exclusivity from Nelson. In this sense, the consummated contracts with the n-1 dealers injure the nth dealer. On still another theory, if the consummated contracts bar entry to potential competitors, Nelson's alternatives to dealing with Motorola are lessened, and his bargaining position worsened when Motorola demands that he too deal exclusively. Is such injury too remote for proximate cause under §§ 3 and 4?

391. This is an argument analogous to a consideration argument occasionally found in charitable subscription cases: each promise to subscribe has its consideration in the other such promises. 1 CORBIN, CONTRACTS § 198 (1950). A similar argument obtains in composition cases. See Johnson v. Parker, 34 Wis. 596, 608 (1874); 6 CORBIN, CONTRACTS § 1283 (1951); 1 WILLISTON, CONTRACTS § 126 (3d ed. Jaeger 1957).

392. Once it is recognized that causation is a public policy notion, "proximate cause" becomes an accordion-like concept which contracts and expands in relation to the interest protected. 2 HARPER & JAMES, TORTS 1132-33 (1956). To be sure, public policy has usually been invoked to limit the scope of liability, see, e.g., Ultramares Corp. v. Touche, 255 N.Y. 170, 174 N.E. 441 (1931), but the principle should work in either direction, see 2 HARPER & JAMES, op. cit. supra at 1133; cf. Summers v. Tice, 33 Cal. 2d 80, 199 P.2d 1 (1948); RESTATEMENT, TORTS § 876(b), comment, illustration 2. Compare Morris, TORTS 195 (1953) (approving Summers v. Tice), with id. at 210 (apparently disapproving policy
A section 1 violation could be based on the seller's efforts to force the would-be buyer to adhere to the restrictive scheme.\textsuperscript{393}

Essential to finding conspiracy under section 1 is the existence of conspirators. Since a single person cannot conspire with himself, no conspiracy can be established \textsuperscript{394} if the seller is a single natural person acting alone. When the seller is a corporation, however, perhaps a combination \textsuperscript{395} or conspiracy can be established. Two theories could be advanced: an intracorporate conspiracy among the corporation's officers or a hub and spokes conspiracy among the corporation and its dealers who submit to exclusivity.

\textit{The Hub and Spokes Conspiracy.} One possible set of conspirators is made up of the seller and its dealers who agree to restrictive contracts.\textsuperscript{396} The dealers, knowing the seller has invited adherence to its scheme, agree to deal exclusively and thus each participate in a conspiracy with the seller to restrain trade.\textsuperscript{397} If these separate "spoke" conspiracies can be aggregated into one "wheel" conspiracy with the seller at the hub,\textsuperscript{398} then the injury to the can-
celled dealer, when he refuses to become another “spoke,” can be said to have been proximately caused by a conspiracy in restraint of trade.

Intracorporate Conspiracy. The intracorporate conspiracy approach to refusal to deal is suggested by Judge Rives in his Nelson dissent and strongly urged by Professor Corbin in his treatise on contracts. There will usually be a plurality of officers involved in the establishment of the set of exclusive contracts which the firm succeeds in imposing on its dealers. As part of this overall plan, the corporate officers and agents attempt to secure the adherence of plaintiff to the trade restraining system. As individuals, each agent is responsible for his acts. But the corporation may also be liable for the

are illustrated by two Supreme Court cases: Kotteakos v. United States, 328 U.S. 750 (1946), and Blumenthal v. United States, 332 U.S. 559-58 (1947). As the Blumenthal case, in distinguishing Kotteakos, indicates, it is not sufficient that each of the exclusive agreements signed by the dealers leads back to Motorola. These agreements can only be aggregated with a single conspiracy if the individual signers are aware that by acceding to Motorola's demand they are “aiding in a larger plan.” Id. at 559.

Would courts impute scienter to dealers—is constructive intent sufficient? The authors have grave misgivings as to the wisdom of this step. Under this theory, there would be a case against every submitting dealer. Or to carry things a little further, every newcomer to the California gasoline market who found himself injured in his business, because he could wrest away but an insignificant share of the market from the majors, would have a case against every gasoline retailer who agreed to exclusivity. While the danger of such suits may be more imagined than real, their possibility shows the dangers of the hub and spokes approach to the case. While it might be attractive to say that courts could hold Motorola liable as a conspirator but let the dealers off the hook on policy principles, the law of conspiracy is otherwise. See Williams, Criminal Law 537-38 (1953).

399. 200 F.2d at 916 (Rives, J., dissenting). "Whether the purpose and effect of the action of these officers and agents were such as to be forbidden by the statutes was the real question to be decided, a question that did not turn on the fact that these officers and agents were acting within the corporate form." 6 Corbin, Contracts § 1417 (Supp. 1958). In commenting on another intracorporate conspiracy case, Professor Corbin observes, "The court puts emphasis on the fact that the defendant is a corporate 'entity' and cannot 'conspire' with itself. It is also a fact that such an 'entity' cannot 'conspire' at all, but it can be held for the conspiracy of its 'agents, servants and employes.'" Ibid.; see Kramer, Does Concerted Action Solely Between a Corporation and Its Officers Acting on Its Behalf in Unreasonable Restraint of Interstate Commerce Violate Section 1 of the Sherman Act, 11 Fdn. B.J. 130 (1951), urging that courts not focus their attention on "conceptual considerations having no relation to economic fact." Id. at 142.

400. It is submitted that they are liable despite the fact that they do not directly profit, a fact which was given weight by the Nelson court. 200 F.2d at 914. See also Arthur v. Kraft-Phenix Cheese Corp., 26 F. Supp. 824, 830 (D. Md. 1938) (cited as authority in Nelson). But the weight of authority is that corporate officers are liable for unlawful acts they commit, irrespective of whether the act personally profits them. See, e.g., United States v. Bach, 151 F.2d 177 (7th Cir. 1945) (corporate agent held liable for violation of price controls on behalf of corporation); Kentucky-Tennessee Light & Power Co. v. Nashville Coal Co., 37 F. Supp. 728, 738 (W.D. Ky. 1941), aff'd sub nom. Fitch v. Kentucky-Tennessee Light & Power Co., 136 F.2d 12 (6th Cir. 1943) (price discrimination, same). See also § 14 of the Clayton Act, making corporate officers criminally liable for corporate Sherman Act violations. See generally Williams, Criminal Law 686-90 (1953). Query: Are the antitrust laws different from other criminal or tort laws in that conspiracy to violate them is excusable if the motive is to benefit another altruistically?
legal consequences of their activity under the doctrine of respondeat superior.\textsuperscript{401} Hence, by invoking the plurality of its agents, the corporation may be held in damages for conspiracy to restrain trade.

The celebrated footnote 59 of Socony-Vacuum declares that section 1 strikes down the contract, combination or conspiracy, “whether the concerted activity be wholly nascent or abortive on the one hand, or successful on the other."\textsuperscript{402} Hence, for example, the conspiracy to fix prices violates section 1 “though no overt act is shown, though it is not established that the conspirators had the means available for accomplishment of their objective. . . .” In refusal to deal cases, the seller’s behavior may go far beyond “mere preparation” and come “dangerously close” to fulfillment.\textsuperscript{403} The only remaining overt act for a full-blown restraint of trade to exist would be the assent of the prospective buyer. If the assent is withheld, the conspiracy among the corporate agents remains nascent and abortive, but if the assent is granted, the conspiracy is complete. Under the doctrine of Socony-Vacuum, the conspiracy would violate section 1 either way.\textsuperscript{404}

Another problem which remains under the intracorporate conspiracy approach to refusal to deal is that of proximate cause. Has the would-be buyer been “injured in his business or property by reason of anything forbidden in the antitrust laws”? Surely, the buyer is “injured” when the corporate officers refuse to deal with him for the reason that he will not join their conspiracy in restraint of trade, irrespective of whether the consummated sales to others injure him. But is the injury “by reason of anything forbidden in the antitrust laws”? If intracorporate conspiracy can violate section 1 of the Sherman Act, then the statutory requirement is met. This theory of injury differs significantly from the section 3 theory previously advanced in that here the aggregate of consummated sales contracts in restraint of trade has been introduced not as the proximate cause of plaintiff’s injury itself, but rather only as evidence of the basic illegality of the corporation’s scheme. That is, the coverage of the market by defendant’s contracts shows their actual or potential anticompetitive effect, \textit{i.e.}, that they are “forbidden by the antitrust laws” as section 4 requires. By shifting the legal locus of the consummated sales from “by reason of” to “forbidden by the antitrust laws,” the proximate cause problem the Nelson court saw for section 3 is avoided.

The theory of conspiracy between the agents of a corporation has been attacked by the \textit{Report of the Attorney General’s Committee}. Approving the Nelson majority’s rejection of intracorporate conspiracy, and disapproving two earlier circuit court opinions which found such conspiracies, the \textit{Report} states that banning the intracorporate “conspiracy” would lead to the unwholesome

\textsuperscript{401} See \textit{Williams, Criminal Law} 683 (1953).

\textsuperscript{402} United States v. Socony-Vacuum Oil Co., 310 U.S. 150, 224 n.59 (1940).

\textsuperscript{403} See People v. Miller, 2 Cal. 2d 527, 531, 42 P.2d 308, 310 (1935); People v. Rizzo, 246 N.Y. 334, 337, 158 N.E. 888, 889 (1927), the two leading cases on criminal attempts.

\textsuperscript{404} For what this is worth in a damages case, it would appear that there is also a violation of the federal conspiracy statute, 18 U.S.C. § 371 (1952).
result that "many activities of any business could be interdicted were joint action solely by the agents of a single corporation acting on its behalf itself held to constitute a conspiracy in restraint of trade."\textsuperscript{405} But this argument proves too much; intracorporate conspiracy between corporate agents is hardly a stranger phenomenon than the well-recognized conspiracy between a parent corporation and a wholly owned subsidiary.\textsuperscript{406} The real question is whether the accused business activities ought to be interdicted, because they restrain trade. Would public policy be better served by striking down the "single person" fiction as applied to that unique legal person, the corporation? It is the belief of the authors that the narrow reading of conspiracy under section 1 is undesirable insofar as it insulates from antitrust sanctions activity which inhibits competition.

But the authors suggest that outside the refusal to deal area the doctrine should be applied with the utmost caution. Certainly, it should not be applied to per se situations; otherwise, to give one illustration, every corporate refusal to deal would constitute a "boycott," illegal per se.\textsuperscript{407} Furthermore, even beyond the per se area, is the doctrine of intracorporate conspiracy not "limited by the neighborhood of principles of policy,"\textsuperscript{408} traditionally associated with section 2 of the Sherman Act? Perhaps the unreasonable restraint standard of section 1, bolstered by intracorporate conspiracy, would usurp the province of the narrower section 2 in dealing with a single powerful firm. A doctrine, once it has come into life, tends to disregard its ancestry and to "declare . . . [itself] absolute to its logical extreme."\textsuperscript{409} The possible conflict between the intracorporate conspiracy doctrine and section 2 should be faced squarely and openly.


\textsuperscript{406} The \textit{Report}, at 34-35, does not, however, object to the use of § 1 against parent and subsidiary corporations which restrain the trade of others. Perhaps, in this view, had Motorola and a subsidiary, say "Motorola Sales Corporation," conspired to secure Nelson's adherence to the system, there would be a violation. See United States v. General Motors Corp., 121 F.2d 376 (7th Cir. 1941), \textit{cert. denied}, 314 U.S. 618 (1941) (GM-GMAC). (The \textit{Report}, at 35, regards \textit{GMAC} as "more a case of contract than conspiracy.")

\textsuperscript{407} Compare United States v. New York Great Atl. & Pac. Tea Co., 173 F.2d 79, 82-83 (7th Cir. 1949). By the same token, whenever a corporation set the price of its product, it would be guilty of "price-fixing."

\textsuperscript{408} See Hudson County Water Co. v. McCarter, 209 U.S. 349, 355 (1908) (Holmes, J.).

\textsuperscript{409} See \textit{ibid.} But "the tendency of a principle to expand itself to the limit of its logic may be counteracted by the tendency to confine it within limits of its history." \textsc{Cardozo, The Nature of the Judicial Process} 51 (1921).
Such jurisprudential considerations may help to explain the Nelson court's rejection of intracorporate conspiracy. For these reasons, courts which see a need to accord antitrust relief to the dealer in Nelson's position may prefer the hub-and-spokes or section 3 approach. Although the former theories require more "fancy doctrinal footwork" than the straightforward intracorporate approach, they pose less possibility of unexpected results elsewhere in the law, and thus are in the pragmatic, "interstitial legislation" tradition of the common law.

To sum up, the wording of the antitrust statute does not necessarily prevent a court from allowing recovery to a dealer injured by an anticompetitive exclusive-dealing system policed by a refusal to deal. But it must constantly be kept in mind that the authors, in advancing this criticism of the Nelson formula, do not intend to abandon the injury to competition standard. They agree with the existing case law: individual refusals to deal are not actionable so long as the consuming public is not injured, even if the cancelled dealer is injured. No injury to the general public is present when close substitute products or sources are readily available.410

But a dealer's suit should not be dismissed on the pleadings. He should be able to introduce evidence as to lessening of competition. To be sure, there is always the danger that the manufacturer who refuses to deal for legitimate reasons will be subjected to harassment by strike suits, but this inconvenience is not too high a price to pay for vindication of the antitrust law by private action—the underlying policy of section 4.

The Klor's Case

At one time, courts regularly dismissed complaints for failure to plead public injury, which was considered an essential part of the section 4 cause of action.411 More recently, the problem has been treated in more sophisticated terms: public injury has been abandoned as a pleading requirement under section 4, a statute whose literal text has no such requirement. The present


Although the foregoing have been considered pleading cases, they contain a hard nub of substantive law. "... [S]ubstantive law has ... the look of being gradually secreted in the interstices of procedure. ..." MAINE, EARLY LAW AND CUSTOM 389 (1836). The authority of these cases, as pleading decisions under the liberal Federal Rules, has been shaken by Radovich v. National Football League, 352 U.S. 445 (1957).
position is that the public injury requirement is inherent in the substantive antitrust laws themselves; absent a per se violation, no unlawful restraint of trade can be found unless there is a "restraint injurious to the public." The recent case of Klor's, Inc. v. Broadway-Hale Stores, Inc. strikingly illustrates the problems inherent in this position.

Plaintiff Klor's was a retail dealer in home appliances in the Mission District of San Francisco; defendant Broadway-Hale is a chain of department stores in California, one of whose outlets is close to the Klor's site. A quarrel arose between the two, the cause of which was not disclosed in the pleadings. As a result, Hale informed its suppliers that if they continued to sell to Klor's, Hale would cease carrying their goods. When the suppliers cut Klor's off, Klor's sued them and Hale for treble damages under sections 1 and 2.

Defendants moved for summary judgment on the ground that no possible anticompetitive effect could have resulted from the acts alleged. In support of the motion, defendants introduced listings of the San Francisco retailers carrying the defendant-manufacturers' products, and fifteen pages of the telephone directory, listing hundreds, or perhaps thousands, of dealers in San Francisco selling home appliances. Plaintiff introduced no counter-affidavits and chose to rely on his complaint. The district court granted summary judgment in a terse opinion denying that any possibility of anticompetitive effect existed.

413. Ibid.
414. 255 F.2d at 219.
415. According to the district court, "it is purely a private quarrel, . . . arising out of some undisclosed cause—the nature of which we may suspect, but do not know." 1956 Trade Cas. 72048 (N.D. Cal.). It has been suggested that Klor's was a price-cutter. Note, 68 YALE L.J. 949, 956 & n.45 (1959) ; Brief for the United States as Amicus Curiae, pp. 9-10. However, on oral argument before the Supreme Court, counsel for defendant denied that there was any attempt to eliminate a price-cutter from the market: "... [W]e raised this point immediately in the district court and the plaintiff never attempted to show a price cutting case. . . . It was never argued by my opponent in the district court or in the court of appeals that this is a price-fixing case." 27 U.S.L. WEEK 3241 (1959).
416. The complaint originally contained other counts, but the pretrial order limited the proceedings to the Sherman Act charges. 255 F.2d at 220 & n.16. In his complaint, plaintiff alleged that "the defendants, all well knowing the facts herein alleged, have restrained trade . . . by contracting, combining, conspiring together, and each with the other, in restraint and monopoly of trade . . ." Id. at 219 n.13. Plaintiff further alleged that Hale had "used its monopolistic buying power to deny to plaintiff its competitive position in the market . . . [and had] purchased . . . the products of the manufacturer-distributor defendants upon the condition that [they] . . . do not sell their products to plaintiff." Ibid.
417. These dealers sold not only the appliances produced by defendants, but those of their competitors—approximately 90 in number. See 255 F.2d at 223. About 1000 of these outlets carried the goods of the manufacturer defendants. The 15 pages of listings show alternative sources of supply available to the public. The number of competitors of the manufacturer defendants suggests that Klor's may also have had alternative sources of supply.
VERTICAL INTEGRATION

On appeal, the Ninth Circuit affirmed, relying primarily on *Apex Hosiery Co. v. Leader* and the *Times-Picayune* case.

There was no charge or proof that by any act of defendants the price, quantity, or quality offered the public was affected, nor that there was any intent or purpose to effect a change in, or an influence on, prices, quantity, or quality, either directly or indirectly. It is not suggested that either the object or effect of the alleged conspiracy was to create an unreasonable restraint, illegal per se.

The Supreme Court unanimously reversed the lower court decisions and remanded the case to the district court for trial. Mr. Justice Black, writing for eight members of the Court, declared that the complaint adequately pleaded a group boycott, illegal per se under section 1. According to the opinion, no public injury need be proved, given a per se violation. Mr. Justice Harlan's concurring opinion sought to decide the case solely on the basis that a cause of action had been pleaded and that the "respondents' affidavits are not necessarily sufficient to constitute a defense irrespective of what the petitioner may be able to prove at trial."

A Procedural Solution. The Court could have handled *Klor's* in several ways. Mr. Justice Harlan's route probably offers the fewest problems. Given our liberal pleading system, the *Klor's* complaint appears to state a cause of action under the antitrust laws. Defendants' fifteen pages of directory listings do not establish, "beyond the slightest doubt," that no anticompetitive effect could occur which would bring defendants' behavior within the ban of the rule of reason. It does not inevitably follow from the large number of dealers that disciplining one dealer is without effect on market behavior. On trial, Klor's might prove to have been a price-cutter or have otherwise been "unduly competitive." The buoyant effect on price levels of the elimination of the small price cutter who can act as a price leader is well known. Moreover, the elimination of an "unduly competitive" retailer may serve as a threat to other retailers; it may inhibit the vigor of price and service competition, casting a cloud over the whole competitive market. Thus, the motion for summary judgment could have been denied on procedural grounds.

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418. 310 U.S. 469 (1940).
420. 255 F.2d at 230.
421. 359 U.S. at 212. Justice Black also appears to suggest that monopolization or conspiracy to monopolize has been pleaded. Id. at 209, 213.
422. Compare 255 F.2d at 221.
423. 359 U.S. at 211.
424. See Dioguardi v. Durning, 139 F.2d 774 (2d Cir. 1944).
425. See Doehler Metal Furniture Co. v. United States, 149 F.2d 130, 135 (2d Cir. 1945).
427. Note, 68 Yale L.J. 949, 956, 960 (1959). Nor does it follow from the large number of alternative sources of supply which are potentially available to the plaintiff, that...
The Per Se Solution. But the Court rejected this route; instead, it chose to reverse on grounds of substantive law. The court declared that a per se violation of section 1—a group boycott—had been pleaded. The question of actual or probable anticompetitive effect becomes irrelevant in such cases. "As to these classes of restraints . . . Congress had determined its own criteria of public harm and it [is] not for the courts to decide whether in an individual case injury had actually occurred." Thus, the conclusive per se rule presumption of intent, or incipient tendency, to restrain trade eliminates any necessity to show, additionally, actual or probable public injury.

The Court's reversal and remand to the district court does not settle the substantive issues in Klor's. Plaintiff must still show the existence of the boycott that the Supreme Court held that he had pleaded. The Court declared boycotts illegal per se, but it did not delimit the scope of the category for the lower court. It merely stated: "Group boycotts, or concerted refusals by traders to deal with other traders, have long been held to be in the forbidden category." If plaintiff could show that the manufacturer and distributor defendants actually agreed with one another to refuse to deal with him, he would have no problem. But it is most unlikely that this did occur or that it could be proved. Probably the most that plaintiff could ever establish would be that Hale approached each supplier separately and persuaded him to agree to stop selling to Klor's. Thus, there would be about eighteen agreements between Hale and a supplier that the latter refuse to deal with Klor's. Can these eighteen agreements be aggregated together to form one boycott, (1) if each of the eighteen suppliers does not know that the others have been approached, or even (2) if the eighteen are aware his elimination, and the consequent setting of a disciplinary example, is unlikely. We do not know whether these potential sources are indeed willing to deal with him or whether the loss of the cancelled lines will prevent him from competing effectively. Cf. text at notes supra.

428. 359 U.S. at 211. Here the Court is paraphrasing the holding of Standard Oil Co. v. United States, 221 U.S. 1, 63-68 (1911).

429. The Court takes the position that the violation alleged in the per se suit need not be shown to be detrimental to the public interest: "In this regard the Sherman Act should be contrasted with § 5 of the Federal Trade Commission Act, 38 Stat. 719, as amended, 15 U.S.C. § 45(b), which requires that the Commission find 'that a proceeding by it . . . be to the interest of the public' before it issues a complaint for unfair competition." 359 U.S. at 211-12 n.4. Compare 27 U.S.L. WEEK 3240-41 (1959) (Frankfurter-Lasky colloquy).


431. Compare text at note 420 supra. As for the conspiracy-to-monopolize issue, it seems utterly improbable that Klor's could show Hale intended to monopolize the San Francisco or even Mission District home appliance market. For this reason, no further discussion of the legal problems involved in such a count is offered.

432. 359 U.S. at 212.

433. Actually, only ten agreements would be needed, since eight defendants are distributors for manufacturer defendants.
of the other agreements? Boycott, in the past, has proved an elusive and elastic concept. But it is doubtful that its scope can include such behavior.

Per Se or Not Per Se. Klor's represents the latest phase in the dialectic of per se. Dicta in earlier cases had indicated that the de minimis effect of a per se unreasonable restraint would not exonerate it. Particularly emphatic on this point is the celebrated footnote 59 of United States v. Socony-Vacuum Oil Co.:

[C]onspiracies under the Sherman Act are not dependent on any overt act other than the act of conspiring . . . . It is the “contract, combination . . . or conspiracy, in restraint of commerce” which § 1 of the


435. Compare Theater Enterprises, Inc. v. Paramount Film Distrib. Corp., 346 U.S. 537, 541 (1954), with Milgram v. Loew’s, Inc., 192 F.2d 579, 583 (3d Cir. 1951), cert. denied, 345 U.S. 964 (1953), on the conscious parallelism problem. See generally Att'y Gen. Nat'l Comm. ANTITRUST REP. 36-42 (1955). For the problem of whether each of the eighteen vertical agreements between Hale and a supplier is itself a “boycott” or merely an “induced unilateral refusal to deal,” see Schwing Motor Co. v. Hudson Sales Corp., 138 F. Supp. 899 (D. Md.), aff’d per curiam, 239 F.2d 176 (4th Cir. 1956), cert. denied, 355 U.S. 823 (1957); Packard Motor Car Co. v. Webster Motor Car Co., 243 F.2d 418 (D.C. Cir.), cert. denied, 355 U.S. 822 (1957). The Court’s reference in Klor’s to “concerted refusals by traders” (emphasis added), see text at note 432 supra, seems to indicate accord with Schwing and Packard. However, for an approach aggregating these many agreements to refuse to deal, even if not concerted or consciously parallel on the part of the suppliers, see Note, 68 Yale L.J. 949, 959 (1959) (“wedge,” “pyramid”).

436. In its original form, the per se doctrine was used in price-fixing cases to counter the defense that the price level fixed was reasonable and that, therefore, the restraint effected was not “unreasonable.” See United States v. Trenton Potteries Co., 273 U.S. 392 (1927); Nash v. United States, 229 U.S. 373 (1913); Rex v. Norris, 2 Kny. 300, 96 Eng. Rep. 1189 (K.B. 1758) (common law rule). The doctrine has been expanded to include allocation of territories, group boycotts, and finally tie-ins. Moreover, the function of the doctrine has altered in the course of its evolution. This is illustrated by the language of Justice Black in the Northern Pacific opinion:

[T]here are certain agreements or practices which because of their pernicious effect on competition and lack of any redeeming virtue are conclusively presumed to be unreasonable and therefore illegal without elaborate inquiry as to the precise harm they have caused or the business excuse for their use. This principle of per se unreasonableness not only makes the type of restraints which are proscribed by the Sherman Act more certain to the benefit of everyone concerned, but it also avoids the necessity for an incredibly complicated and prolonged economic investigation into the entire history of the industry involved, as well as related industries, in an effort to determine at large whether a particular restraint has been unreasonable—an inquiry so often wholly fruitless when undertaken.

356 U.S. at 5. This analysis blends two functions of the per se rule: first, on the theory that, since the inevitable future consequence of certain practices is an anticompetitive effect on the market, those who adopt these practices must be conclusively presumed to have intended such consequences, constructive intent is substituted for the actual intent test of the rule of reason. United States v. Standard Oil Co., 221 U.S. 1, 65 (1911). Second, difficult and expensive economic analysis for which courts may be “most ill-suited” is obviated by recourse to a per se rule.
Act strikes down, whether the concerted activity be wholly nascent or abortive on the one hand or successful on the other. . . . [A] conspiracy to fix prices violates § 1 of the Act although no overt act is shown, though it is not established that the conspirators had the means available for accomplishment of their objective . . . .

Yet courts have frequently regarded it desirable to avoid a rigid application of the per se rule against practices they regarded as “necessary and legitimate” from a business standpoint. In such cases, the courts have simply denied that the practices in question belonged in a forbidden category, and have instead chosen to analyze them in terms of the more general Sherman Act prohibitions under the rule of reason. As a result, the border lines of the per se categories have been blurred and their territories pockmarked with enclaves. Predictability in this area has thus been jeopardized.

By apparently introducing a de minimis exception for at least one per se offense, tie-ins, Northern Pacific revealed another method to mitigate the rigors of per se. But in so doing, it may have undermined the whole per se doctrine by opening the door to a general de minimis qualification. Judge Barnes, in the Ninth Circuit Klor’s opinion, appears to have understood Northern Pacific to support a general antitrust requirement of adverse effect on competition. But the Supreme Court’s reversal of Klor’s seems to mark a return to the rule of Socony-Vacuum.

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440. If anything can be said for a per se rule, it is that because it has a constructive intent ingredient, it is a rough substitute for inciency. Intent approximates inciency to the extent that both nip practices in the bud, which, if allowed to mature, would have an anticompetitive effect. But a doctrine suffering so many vicissitudes and leading to so much unpredictability may not be an efficient tool for approximating inciency. The economy and predictability Mr. Justice Black sees in per se, see note 436 supra, may prove illusory.

441. 255 F.2d at 230 n.41a; see Handler, Recent Antitrust Developments, 13 Record of N.Y.C.B.A. 417, 425-27 (1958).

442. The opinion may, however, reveal some reservation on this point by the Court. At the close of his opinion, Mr. Justice Black discusses the “monopolistic tendency” of Hale’s practices:

As such it is not to be tolerated merely because the victim is just one merchant whose business is so small that his destruction makes little difference to the economy. Monopoly can as surely thrive by the elimination of such small businessmen, one at
An Injury to Competitors Solution. The Court could have used still another route to reach its decision, one which the Justice Department seems to have urged as amicus curiae.\textsuperscript{443} Hale's practices could have been condemned, not as per se illegal, but as illegal under the rule of reason, by replacing the rule's public injury test by an injury to competitors test. While the Court declined to adopt this solution there is language in Justice Black's opinion suggesting a willingness, at least on his part, to accept it in a case where the question cannot be avoided by recourse to a per se test.\textsuperscript{444} Whether section a time, as it can by driving them out in large groups. In recognition of this fact the Sherman Act has consistently been read to forbid all contracts and combinations “which ‘tend to create a monopoly,’” whether “the tendency is a creeping one” or “one that proceeds at full gallop.”

359 U.S. at 213-14.

The emphasis on monopoly power here is somewhat reminiscent of the “sufficient economic power... to appreciably restrain free competition” language in Northern Pacific. To the extent that this is an alternative explanation for the decision, thrown in by the Court to buttress the holding, Klor's may not represent a complete swing away from Northern Pacific back to Socony-Vacuum. On the other hand, this language may be interpreted simply to explain the policy of the position that boycotts are illegal per se however insignificant the victim.

443. See Brief for the Government on Petition for Certiorari, pp. 3-6 (argued under rule of reason, not per se); Main Brief for Government, pp. 3 (question presented), 7-11 (not per se), 11-13 (\textit{Apex}).

444. The court below relied heavily on \textit{Apex Hosiery Co. v. Leader}, 310 U.S. 469, in reaching its conclusion. While some language in that case can be read as supporting the position that no restraint on trade is prohibited by §1 of the Sherman Act unless it has or is intended to have an effect on market prices, such statements must be considered in the light of the fact that the defendant in that case was a labor union. The Court in \textit{Apex} recognized that the Act is aimed primarily at combinations having commercial objectives and is applied only to a very limited extent to organizations, like labor unions, which normally have other objectives. See \textit{United States v. Hutcheson}, 312 U.S. 219; \textit{Allen Bradley Co. v. Local 3, International Brotherhood of Electrical Workers}, 325 U.S. 797. Moreover, cases subsequent to \textit{Apex} have made clear that an effect on prices is not essential to a Sherman Act violation. See, e.g., \textit{Fashion Originators' Guild v. Federal Trade Comm'n}, 312 U.S. 457, 466. 359 U.S. at 213 n.7. (Emphasis added.) See also the Frankfurter-Lasky colloquy at oral argument, 27 U.S.L.W. 3241 (1959). The Justice Department's amicus curiae main brief strongly urges that \textit{Apex} be treated as merely a labor case. Pp. 11-13; see Brief for the United States on Petition for Certiorari, p. 4 n.3.

While \textit{Apex} was a labor case, Mr. Justice Stone did not regard his decision to state a rule applicable only in the labor context:

Apart from the Clayton Act [§§ 6, 20] it [the Sherman Act] makes no distinction between labor and non-labor cases. We only hold now, as we have previously held both on labor and non-labor cases, that such restraints are not within the Sherman Act. ... Unless the principle of these cases is now to be discarded, an impartial application of the Sherman Act to the activities of labor and industry alike would seem to require that the Act be held inapplicable....

310 U.S. at 512. Nevertheless, in its historical perspective, the result in \textit{Apex} was an important preliminary step toward removing labor cases from antitrust jurisdiction. Its
1 is to utilize only an injury to competition standard, or is to include injury to competitors as well is not answered by the Klor's decision. In the guise of a per se rule, however, "injury to competitors" may have entered by the back door.

The Policy of Section 4: Antitrust as Tort

The notion of injury to competitors has played an important role in early antitrust cases and in the legislative history of the Sherman Act. It was only gradually that injury to competition evolved as the dominant theme. But the opposing theme has, as we have seen, not disappeared. For the FTC, injury to competitors has long been a principal standard of judging the

halfway solution to the problem was abandoned the following year in the Hutcheson case, supra, which completely ousted antitrust from "labor disputes." (Allen Bradley, supra, then helped define the scope of "labor disputes." ) Moreover, other antitrust decisions dealing with labor have been distinguished away by the Court. See, e.g., United States v. Frankfort Distilleries, Inc., 324 U.S. 293, 297-98 (1945) (local commerce, interstate commerce, interpreted differently in labor, business settings) (Black, J.) But see id. at 298 (follows Apex). Thus, were Apex the sole authority for the public injury rule, its strength as a precedent might be weak. However, the public injury rule of Apex is followed in the leading Supreme Court § 1 rule-of-reason cases. See Times-Picayune Publishing Co. v. United States, 345 U.S. 594 (1953); United States v. Columbia Steel Co., 334 U.S. 495 (1948). Moreover, the courts of appeals have uniformly applied this test in the cancelled-dealer antitrust suits. See Kessler, Automobile Dealer Franchises: Vertical Integration by Contract, 66 YALE L.J. 1135, 1166-67 & nn.204, 207, 212 (1957) (collecting cases). The Fashion Originator's Guild case, cited by Mr. Justice Black for the proposition that price effect "is not essential to a Sherman Act violation" merely, as the authors read it, enunciates the incipiency doctrine under the FTC Act. See 312 U.S. at 466. But cf. id. at 467 (quotation of injury to competitors dictum from very early Sherman Act price-fixing case).

The lower court opinion in FOGA, 114 F.2d 80, 85 (2d Cir. 1940), however, did contain extremely strong injury-to-competitors language: "[T]he interest of the consumer is not all that determines the 'reasonableness' of the contract 'in restraint of trade.' It is also unlawful to exclude from the market any of those who supply it . . . and it is no excuse for doing so that their exclusion will result in benefits to the consumer . . . ."


446. Mr. Justice Holmes claimed that the Sherman Act was passed not so much to protect competition as to protect traders from competition. "The court below argued as if maintaining competition were the expressed object of the act. The act says nothing about competition. I stick to the exact words used . . . . It was the ferocious extremes of competition with others, not the cessation of competition among the partners that was the evil feared." Northern Secs. Co. v. United States, 193 U.S. 197, 403-05 (1904) (dissent). See also United States v. Trans-Missouri Freight Ass'n, 166 U.S. 290, 323-26 (1897). Whether or not the common law cases supported the Holmes view, see Adelman, Book Review, 46 AM. ECON. REV. 481, 486 (1956), the majority of his colleagues on the Court did not agree with him. The act which "says nothing about competition" is now generally considered to have as its general objective "the promotion of competition in open markets." ATT'Y GEN. NAT'L COMM. ANTITRUST REP. 1 (1955).
unfairness of methods of competition. In at least one Justice Department Sherman Act prosecution against a vertical integration system, the case was based largely on this theory. And, in its amicus curiae brief in Klor's, the Department came out strongly in favor of injury to competitors as sufficient for the existence of a Sherman Act violation, irrespective of the presence or absence of injury to competition.

The chief objection to making injury to competitors an alternative standard of antitrust illegality is that the consequence may be to inhibit competition itself. This has already been recognized to be a serious problem in the Robinson-Patman Act context. Allowing injury to competitors, in itself, to be a criterion of antitrust illegality in the vertical integration context would probably have an anticompetitive effect, since every vertical integration arrangement injures those competitors excluded from the business involved. To deprive industry of the economies of integration in order to prevent such injury would thus be to exalt protection of competitors over competition. Under our free enterprise system, the premise is "that the unrestrained interaction of competitive forces will yield the best allocation of our economic resources, the lowest prices, the highest quality and the greatest material progress . . . ." Is protection of com-


449. See note 443 supra. See also Loevinger, Private Action—The Strongest Pillar of Antitrust, 3 ANTITRUST BULL. 167, 175 (1958).

450. See BOULDING, ECONOMIC ANALYSIS 725-26 (3d ed. 1955). Boulding suggests that if compensation is to be given to the competitor injured by competition, it should be charged to society as a whole rather than an individual defendant and no attempt should be made to freeze the economic structure. Ibid.


452. Indeed any contract restrains someone's trade because outsiders are excluded from the business which is the subject of the contract. The problem is: Is the restraint unreasonable? Standard Oil Co. v. United States, 231 U.S. 1, 63 (1911).

453. Northern Pac. Ry. v. United States, 356 U.S. 1, 4 (1958) (Black, J.). See also ATT'Y GEN. NAT'L COMM. ANTITRUST REP. 317 (1955); BOULDING, op. cit. supra note 450, at 607-08, 654-60. Compare STIGLER, THE THEORY OF PRICE 213-14 (rev. ed. 1956). It would appear that we may substitute for Mr. Justice Black's expression "greatest material progress," the utilitarian notion of greatest good of (or goods for) the greatest number. However, the passage quoted continues, "... while at the same time providing an environment conducive to the preservation of our democratic political and social institutions. But even were that premise open to question, the policy unequivocally laid down by the act is competition." 356 U.S. at 4. Perhaps, the passage could be interpreted to endorse the benefits of competition except when our democratic political and social institutions are threatened
petitors worth the sacrifice of these benefits of competition to society?454

A Compromise Solution? But an adherent of an injury to competitors test might reply that this statement of the issue oversimplifies the differences between two great principles. The injury to competitor principle, he will admit, if carried to the extreme, will destroy competition.455 But this does

by injuries suffered by competitors as a result of the vigor of competition. Compare the Douglas dissent in Standard Stations, text at note 101 supra. However, it is more probable that Mr. Justice Black merely intended to equate best allocation of resources and greatest material progress with the environment most conducive to the preservation of our institutions, or else that both effects inevitably flow from competition.

454. For a view that co-existence is possible, see Adelman, Integration and Antitrust Policy, 63 Harv. L. Rev. 27, 77 (1949). Another possibility is that the two standards will not coexist as separate alternatives, but that courts will require both types of injury to be proved in all cases. This could hamper Government intervention in cases where competition was inhibited, to the satisfaction of all competitors already in the market, but without injury to any of them. See United States v. Socony-Vacuum Oil Co., 310 U.S. 150 (1940).

455. Moreover, extension of antitrust into a host of private commercial grievances could result in so many different problems being dealt with by one body of law that general principles would be obfuscated in a maze of case-by-case analysis. At the same time, we may doubt the propriety of use of antitrust as a cumulative federal tort remedy for the state-law tort of unfair competition.

Perhaps, the policy of the antitrust laws, as reflected in their wording, is sufficiently foreign to tort policies as to make antitrust an inefficient means of regulation of unfair business practices. If we are to have a federal law of unfair competition, Congress should frame a comprehensive scheme for it. To some, Lanham Act §§ 43(a), 44(h)-(i), 60 Stat. 441 (1946), 15 U.S.C. §§ 1125(a), 1126(h)-(i) (1958), already embody a comprehensive federal unfair competition law. Robert, Commentary on the Lanham Trade Mark Act, 15 U.S.C.A. 265, 283-86 (1948); Robert, The New Trade Mark Manual 177 (1947); see Ross-Whitney Corp. v. Smith Kline & French Labs., 207 F.2d 190, 193-94 (9th Cir. 1953) (dictum); Pagliero v. Wallace China Co., 198 F.2d 339, 341 (9th Cir. 1952); Stauffer v. Exley, 184 F.2d 962 (9th Cir. 1950); In re Lyndale Farm, 38 C.C.P.A. (Patents) 825, 186 F.2d 723 (1951). Contra, Royal Lace Paper Works, Inc. v. Pest-Guard Prods., Inc., 240 F.2d 814 (5th Cir. 1957); Arttype, Inc. v. Szapulla, 228 F.2d 695 (2d Cir. 1956); L'aiglon Apparel, Inc. v. Lela Lobell, Inc., 214 F.2d 649, 651-54 (3d Cir. 1954); American Auto. Ass'n v. Spiegel, 205 F.2d 771 (2d Cir.), cert. denied, 346 U.S. 887 (1953); Ramirez & Ferand Chile Co. v. Las Palmas Food Co., 146 F. Supp. 594, 603, aff'd per curiam, 245 F.2d 874 (9th Cir. 1957). See also Iowa Farmer's Union v. Farmers' Educ. & Co-op Union, 247 F.2d 809, 819 (8th Cir. 1957). For policy considerations, see generally Maternally Yours v. Your Maternity Shop, 234 F.2d 538, 545-46 (2d Cir. 1956) (concurring opinion); Hyde Park Clothes v. Hyde Park Fashions, 204 F.2d 223, 226 (2d Cir.), cert. denied, 346 U.S. 827 (1953); Note, 60 Harv. L. Rev. 1315 (1947); Chafee, Unfair Competition, 53 Harv. L. Rev. 1289, 1298-1301 (1940).

Moreover, aside from the inefficiency engendered by utilizing antitrust as a means of regulating unfair competition or unfair methods of competition, the propriety of so using antitrust may also be questioned. With respect to labor torts, the Court has declared, “The maintenance in our federal system of a proper distribution between state and national governments of police authority and of remedies private and public for public wrongs is of far-reaching importance. An intention to disturb the balance is not lightly to be imputed to Congress.” Apex Hosiery Co. v. Leader, 310 U.S. 469, 513. Until Congress declares its intentions in this area, perhaps the wiser course would be federal inaction rather than action.

Query: Should state tort law aimed at protection of competitors so evolve as itself to
not mean that we have to place sole reliance on injury to competition. Both standards can be so modified as to bring about this reconciliation: Injury to competitors should be prevented unless the result is injury to competition. Under this formula an injured competitor could recover unless it could be shown that his recovery would destroy an integration system which is beneficial to competition.

An Addyston Pipe Solution? Despite the superficial attractiveness of the proposal, an evaluation of its consequences dictates its rejection, at least in the crude form in which it has been phrased. Clearly, not every contract or acquisition which restrains the trade of a competitor should be forbidden. Unsuccessful rivals are always injured when they lose business. To require a defendant to justify his integration arrangements, or business arrangements in general, in terms of positively promoting competition would put an intolerable restriction on freedom of contract and freedom of acquisition. The problem is to define which contracts and acquisitions "unreasonably" injure them. Is it possible to define a rule of reason which protects competitors more fully than the rule of Apex, but which does not intolerably hamper freedom of contract and acquisition? Perhaps such a standard already exists in United States v. Addyston Pipe & Steel Co., where Judge (later Chief Justice) Taft enunciated the common-law rule for unreasonable restraints of trade; contracts in restraint of trade are not lawful unless "ancillary to the main purpose of a lawful contract, and necessary to protect the covenantee in the enjoyment of the legitimate fruits of the contract . . .." This standard is akin to the now-disused formulation of the rule of reason that restraints are reasonable if adopted for good business reasons. The important difference is, however, that under the proposed formulation, good business reasons are necessary for exoneration, rather than sufficient.

Were the rule of Addyston Pipe revived, serious difficulties would exist in adjusting a contract standard to ownership integration situations, but such problems are not insurmountable. Even graver problems are raised with respect to the substantive content of the terms "necessary" and "legitimate fruits" and the risk of nonpersuasion in such cases. Certainly any practice which is anticompetitive as well as anticompetitor is neither necessary nor are the fruits it secures legitimate. However, once we leave the realm result in injury to competition, would a burden on commerce exist? Is the field preempted by the Sherman Act? Compare Parker v. Brown, 317 U.S. 341 (1943), with Schwegman Bros. v. Calvert Distilleries Corp., 341 U.S. 384 (1951). Cf. Capitol Records, Inc. v. Mercury Records Corp., 221 F.2d 657 (2d Cir. 1955) (L. Hand, J., dissenting: "publication" must be a federal question).

456. 85 Fed. 271 (6th Cir. 1898), aff’d, 175 U.S. 211 (1899).
457. 85 Fed. at 278-89.
of anticompetitive practices, it becomes extremely difficult to define what
is necessary or unnecessary.\footnote{459} Must this be done on a case-by-case basis\footnote{460} or does the formula itself furnish “a sufficiently uniform standard”?\footnote{461} Probably, the difficulty of developing a workable, nonsubjective content for “necessary” has contributed to the demise of the Addyston Pipe formula and its replacement by the modern rule of reason.\footnote{462} A further difficulty lies in the proper allocation of the burden of persuasion. Once plaintiff introduces evidence of existence of a restrictive practice, need he also prove that the practice is not “necessary”? Or should defendant have the burden of producing evidence of “necessity,” since he is in better control of the relevant facts?\footnote{463} In many cases this may be of critical importance because neither party can prove anything,\footnote{464} or because the cost of gathering evidence is prohibitive.\footnote{465} Such doubts must temper a lingering affection for the rule of Addyston Pipe and, it is submitted, dictate that the case continue to be more honored in the citation than the observance.

The Standard Stations Solution. In the light of the difficulties in framing an injury to competitors rule to supplement the injury to competition standard, the authors submit that the only workable synthesis between the two tests is that already achieved by the Supreme Court in Standard Stations. The authors advocate that the rule of Standard Stations be carried over in its entirety to section 4 cases. Under this rule, there would be a treble damages cause of action by a competitor or dealer\footnote{466} against a vertically integrating

\footnotesize{459. Compare Int. Rev. Code of 1954, § 162 (“ordinary and necessary”) and the vicissitudes of its case law; Note, 68 Yale L.J. 528, 534 n.41 (1959) (trademarks may be allocated among different products when the arrangement serves a “legitimate business purpose,” rather than an anticompetitive one).


462. See Handler, Antitrust in Perspective 12 (1957) (“By freezing the law as it stood in 1890, Taft would have deprived it of all capacity for growth. That is hardly the construction to be given a law of constitutional dimension intended to safeguard our basic economic liberties.”).

463. McCormick, Evidence 641, 675 (1954), suggests that the burden on the party in control of the evidence should be only to bring forward evidence rather than to persuade the trier.

464. See id. at 686; cf. Gray v. Gardner, 17 Mass. 188 (1821); Stern, Buyer Indifference and Secondary Meaning in Trademark and Unfair Competition Cases, 32 Conn. B.J. 388 n.26 (1958). For one solution of the dilemma, see Stone, Burden of Proof and the Judicial Process, 60 L.Q. Rev. 262, 278 (1944), where allocation of the burden is urged to be dictated by probability of culpa, so that justice may prevail a majority of the time.

465. Compare the cost-justification problem in Robinson-Patman Act suits, see text at notes 514-24 infra. If the burden is cast on defendant, may not the juridical risk in adopting integration create a potential clog on competition? See text at notes 450-54 supra.

466. Or supplier, for that matter, should a backward integration analogue to the Nelson case arise. Cf. Mackey v. Sears, Roebuck & Co., 237 F.2d 869 (7th Cir. 1956), petition for cert. dismissed per stipulation, 355 U.S. 865 (1957).}
firm if and only if the integration system does or may substantially lessen competition in the relevant market by erecting barriers to entry.\textsuperscript{467} In their view, only when injury to competitors\textsuperscript{468} rises to the level of injury or prospective injury to competition itself should there be a cause of action under the antitrust laws.

**The Future of Private Action Against Vertical Integration**

Section 4 has been generally unsuccessful as a complement to Government prosecution in the exclusive dealing area. Probably the preferable route to remedy this situation is via evolution of the case law. A judicial case-by-case approach, hammering out a rule slowly, is likely to avoid the drastic and unintended consequences which often attend a blanket prohibition. Moreover, a judge-made rule is more easily altered to meet later needs than is a legislative mandate. Hence, if further development of the existing case law could achieve the desired ends, then it would be better not to tamper with the antitrust laws. But serious obstacles to such development exist, both within the existing case law and the statutes themselves. Moreover, the courts have had ample opportunity to revise their interpretation of the statutes and have evidenced an unwillingness to do so. As a result, pressure for new legislation has mounted. For example, the enactment of the Auto Dealer Day in Court Act was a legislative response to the problems of automobile dealers whose franchises had been cancelled. Suggestions have been made for the extension of this legislation to other industries. Suggestions for more drastic legislation have also been made. In the subsection which follows, this legislation will be discussed and an alternative statutory solution will be proposed.

**The Auto Dealer Day in Court Act**

Cancelled automobile dealers have been among the most vigorous and least successful users of the antitrust laws.\textsuperscript{469} After suffering defeat in the courts, the dealers resorted to another tribunal:\textsuperscript{470} in 1956 they secured passage of the Automobile Dealer Day in Court Act.\textsuperscript{471} The act, according to its preamble, is to “supplement the antitrust laws . . . in order to balance the power now heavily weighted in favor of automobile manufacturers,” and permits auto dealers to recover damages “sustained by reason of the failure of automobile manufacturers to act in good faith in complying with the terms of franchises or in terminating or not renewing franchises.” The duty to act in good faith is defined by the statute as the obligation of the parties to the

\textsuperscript{467}. “Entry” here is to be understood as maintenance of or expansion of existing competitive activity as well as introduction of new competition. Compare BAIN 5.

\textsuperscript{468}. Or dealers or suppliers. See note 466 supra.


\textsuperscript{470}. See id. at 1167-75.

franchise "to act in a fair and equitable manner toward each other so as to guarantee the one party freedom from coercion, intimidation or threats of coercion or intimidation from the other party."\footnote{472}

The Day in Court Act poses serious questions of interpretation. Two phrases used in the statute are crucial—"good faith" and "coercion, intimidation, or threats of coercion or intimidation." In order to determine what standard of behavior the act imposes on the parties, the first question which must be answered is whether the duty to act in good faith is limited to abstention from coercive practices, or whether the duty has some wider scope. In either case, the meaning of "coercion" merits careful exploration. And a very basic problem inherent in the statute is whether the dealer is to be protected even at the expense of curtailing competition.

Good Faith. Section 1(e) of the act defines "good faith" as the duty of each party to the franchise to act in a fair and equitable manner toward the other so as to guarantee him freedom from coercive practice. The words "so as" may be read either as words of qualification, limiting the duty to act in good faith only to abstention from coercion, or else as words of illustration, exemplifying coercion as only one instance of bad faith. The statutory wording is thus inconclusive in determining the scope of the duty.

The original version of the bill passed by the Senate imposed on the manufacturer, in the name of good faith, a duty to act in a fair, equitable, and nonarbitrary manner toward the dealer in order to guarantee him freedom from manufacturer coercion and preserve all the equities of the dealer inherent in the franchise relationship.\footnote{473} The House changed the bill in two ways: the phrase about preserving all the equities was deleted and the duty to act in good faith was imposed upon the dealer as well as upon the manufacturer. The two changes suggest two contradictory interpretations of the scope of good faith. Insofar as the House deleted the phrase defining good faith in terms of preserving all the equities of the dealer, it appears that it was found unnecessary to grant any protection further than guaranteeing freedom from coercion. This would point to correctness of reading "so as" as words of qualification. But imposition of the duty to act in good faith upon the dealer suggests the contrary interpretation. It hardly seems probable that Congress wished to protect automobile manufacturers from dealer coercion.\footnote{474} Yet, if the duty to act in good faith which the act imposes on dealers is a duty limited to abstention from coercion,\footnote{475}


473. S. 3879, § 1(e), 84th Cong., 2d Sess. (1956).

474. The preamble states that the purpose of the act is "to balance the power now heavily weighted in favor of automobile manufacturers." The manufacturer can use lack of good faith on the dealer's part only as a defense to dealer suits.

475. For the likelihood of the occurrence of dealer acts of coercion, see Note, 70 Harv. L. Rev. 1239, 1247-52 (1957); Comment, 52 Nw. U.L. Rev. 253, 259 (1957); Comment,
then this unrealistic conclusion follows as the legislative purpose.\textsuperscript{476} "So as" would then seem to be words of illustration. Thus it is necessary to probe still further to ascertain the scope of "good faith" under the act; the changes by Congress in the wording of the law do not help us.

Turning to the \textit{House Report}, we find one passage which uses language which strongly suggests that coercion is a necessary prerequisite for lack of good faith. In discussing 1(e) the report states that the term "fair and equitable manner" is qualified by the requirement of coercion and that "in each case arising under this bill good faith must be determined in the context of coercion or intimidation or threats . . . ."\textsuperscript{477}

Finally, we must consider the probability that, given a statute which derogates from common law rights of freedom of contract, the courts are likely to interpret the statute restrictively, despite its declared remedial purpose. Hence, the weight of decision will probably incline toward restricting the duty to act in good faith solely to the abstention from coercive practices.

\textit{Coercion}. The crucial question, then, is: What is the meaning of "coercion"? Minimally the term encompasses intimidation or predatory behavior. Sending a dealer cars of the wrong color or in the wrong quantity, or threatening to drive him out of business if he refuses to accede to manufacturer

\textsuperscript{9} \textit{Stan. L. Rev.} 760, 770 (1957). The \textit{Harvard} note, \textit{supra} at 1248 n.72, gives an instance of dealer "coercion" of a manufacturer, \textit{Webster Motor Car Co. v. Packard Motor Car Co.}, 135 F. Supp. 4 (D.D.C. 1955) (dealer Zell threatened Packard that he would quit unless Packard cancelled dealer Webster and made Zell the only franchised dealer in area; Webster sues Packard under §§ 1-2 for acceding to Zell demand). The authors prefer the position suggested by the appellate court in subsequently reversing the cited case. \textit{Packard Motor Car Co. v. Webster Motor Car Co.}, 243 F.2d 418 (D.C. Cir. 1957). The court there held that Webster had no treble damages cause of action against Packard because the cancellation was "reasonable." First, there was no adverse competitive effect because of the effective competition by other makes and other dealers. Second, there \textit{would be} an anti-competitive effect were Packard not permitted to retain its largest dealer at the price of cancelling a less important one. Since Packard's behavior was not an unlawful restraint of competition, it would appear that Zell's was not, either. Thus, Zell did not "coerce" Packard within the meaning of the act. (\textit{Query}: Was this an allocation of territories governed by a per se rule? See note 504 \textit{infra}. \textit{Klor's} suggests that there is \textit{no de minimis} escape hatch in per se cases. \textit{Klor's} probably does represent an instance, outside the automobile field, of coercion of manufacturers by a powerful dealer.)

An interesting problem in statutory construction would have been raised if the \textit{Webster} case had arisen under the Day in Court Act, and if the assumption be made that Zell did "coerce" Packard into action which would have an anticompetitive effect. Would Webster now have a cause of action against Packard? Packard did not directly coerce Webster for its own purposes. But Packard did act as the conduit for Zell's coercive behavior. Section 1(e) does not specify whether the coercion must originate with defendant or may also originate with another party. Perhaps, on an agency or conspiracy theory, Webster might succeed in holding Packard liable for acceding to Zell's coercive demand.

\textsuperscript{476} Another possibility is to give one meaning to "good faith" when considering the dealer's duty and another when considering the manufacturer's, but this would seem unjustified by the wording of § 1 (e).

demands, are in all probability coercive acts under the statute. But is such behavior the outer limit of "coercion" under the act? 478

As in the case of "good faith," the wording of the statute itself is inconclusive; "coercion" is not expressly defined. The legislative history, however, points to a broader meaning of "coercion," which would include disciplinary cancellation. In discussing section 2(e), the House Report emphasizes that "in each case arising under the bill good faith must be determined in the context of coercion or intimidation or threats of coercion and intimidation." 479

This indicates that practices can be "coercive" without being actually "intimidating." The Report further states that:

The manufacturer's obligation to act in good faith (e.g., not cancel) extends to all of his franchised dealers, including: dealers who sell automobiles to other dealers, franchised or not, for resale to the public; dealers who sell outside of a "zone of influence" or "territory"; and dealers who sell automobiles at less than the manufacturers' suggested resale prices. Contract provisions restricting an automobile dealer from transacting business with customers of his choice, or from selling outside a specified territory could violate the antitrust laws. Any restriction on a dealer's right to sue based on the fact that he is selling to another dealer, franchised or not, for resale to the public or based on the fact that he sells outside of a territory or sells at set rates would contravene the congressional purposes underlying section 4 of this bill which provides that this measure shall not repeal, modify, or supersede, directly or indirectly, any provision of the antitrust laws. 480

478. It is the authors' position that the meaning of "coercion" is as follows: X coerces Y means: (1) X offers Y the choice of doing X's bidding or else being subjected to some sanction; and (2) X has the power to exercise the sanction against Y; but (3) for X to exercise the sanction against Y is not lawful, or for Y to do as X bids would serve an unlawful end of X. "Lawful," as used here, refers to the laws of the United States other than the Day in Court Act, including criminal, tort, and contract law. That threat to breach a contract constitutes coercion ("economic duress") is amply supported by the authorities which hold that extra compensation extracted to avoid a breach is unsupported by consideration. See Dawson & Harvey, Cases on Contracts and Contract Remedies 743-50 (1959) (collecting authorities). Note: the second clause of (3) may be subsumed by the first.


The existence of coercion or intimidation depends upon the circumstances arising in each particular case and may be inferred from a course of conduct. For example, manufacturer pressure, direct or indirect, upon a dealer to accept automobiles, parts, accessories, or supplies which the dealer does not need, want or feel the market is able to absorb, may . . . constitute coercion or intimidation. Similarly coercion or intimidation may be found where the manufacturer attempts to require the dealer to handle exclusively, or sell a specified quota of parts, accessories, and tools made or approved by the manufacturer.

If the evidence discloses normal sales recommendation or persuasion the manufacturer would not be liable. On the other hand, if the manufacturer goes beyond normal sales recommendation or persuasion . . . his activities could give rise to a cause of action under the bill . . .

Ibid.

480. Id. at 10.
In the light of the foregoing, the emphasis on coercion becomes understandable. Among the chief targets, if not the chief targets of the act, are the informal exclusive arrangements which do not appear in the franchise and which are enforced by cancellation or nonrenewal, or threats of such action. Such coercive practices already constituted violations of the antitrust laws when they effected a substantial lessening of competition, an unreasonable restraint of trade, or an unfair trade practice or method of competition, but they could be attacked only by the Department of Justice or the FTC, and grave evidentiary problems existed. The dealer injured by coercive cancellation or nonrenewal was given no effective private cause of action under the customary interpretation of section 4 of the Clayton Act. Under the new act, an auto manufacturer who fails to renew a recalcitrant dealer can no longer find refuge in the doctrine that, by refusing to deal, he is merely invoking his inalienable right to trade with whom he pleases. Nor can the absence of a consummated antitrust offense bar suit. In this respect the Dealer Act goes indeed beyond the existing antitrust law, supplementing it as the preamble asserts.481

Impact of the Act on Competition. It might be argued that the act has deliberately sacrificed a basic tenet of antitrust policy, the prevention of injury to competition. Critics of the legislation may claim that Congress, in its solicitude for the dealer, has granted him a local monopoly, and has built up the countervailing power of the dealer against the manufacturer to such an extent as to create more serious market problems than existed before.482 That this was the intention of Congress is not borne out by the legislative history of the act. The House Report declares that the phrase in the Senate bill which required the manufacturer to act so as to preserve all the equities of the dealer inherent in the franchise relationship was deleted by the House "to preclude any interpretation inconsistent with antitrust principles."483 And section 4 of the act, which states that the act is not intended to repeal the antitrust laws, becomes even more meaningful in the light of the following commentary in the Report: "The bill . . . does not prohibit the manufacturer from terminating or refusing to renew the franchise of a dealer who is not providing the manufacturer with adequate representation. Nor does the bill curtail the manufacturer’s right to cancel or not to renew an inefficient or undesirable dealer’s franchise."484 Other passages even more powerfully underscore the antitrust orientation of the act. According to the Report, pro-

481. To the extent that intimidatory practices are outlawed, competitive effect vel non, the act does not have solely antitrust policy purposes, but a tort aim as well. Thus, Congress has to this extent established a new federal tort, outside the scope of the Clayton Act § 4 tort. However, it should be noted that the dealer receives only single damages under the Day in Court Act rather than treble damages as under § 4. The Senate bill, supra note 473, proposed double damages.
482. See note 486 infra.
484. Id. at 9.
tection will be accorded to a dealer engaged in cross-selling or bootlegging, and it is emphatically stated that "the bill does not freeze present channels or methods of automobile distribution" nor does it "afford the dealer the right to be free from competition." Thus, the legislative history shows that it was not the intention of Congress to hinder competitive automobile retail distribution.

Nevertheless, despite the assurance the House Report gives, in practice the act may freeze present channels and methods of distribution and restrain manufacturers from removing inefficient dealers. Once sued, unless the manufacturer can secure a verdict on the pleadings or a directed verdict, he must run a grave juridical risk. Hence, the act may function in terroram, and while it may inhibit borderline coercive behavior, at the same time it could inhibit manufacturers from eliminating inefficient elements in their distribution system.

To the extent that the latter occurs, inflexibility in automobile distribution would be increased. Nevertheless, this result does not compel the conclusion that the act goes too far. Any remedial legislation is bound to create new juridical risks. The question of whether the act creates more problems than it solves is one of fact which only experience can answer. The workability of the law will depend on the ability of the judiciary to apply the statute in a manner which accords the dealer a greater degree of independence without destroying manufacturer and consumer interests in an efficient dealership system.

The interpretation the courts give to the term "coercion" in the act will probably prove the key to the effect of the new law on the market. The

485. The bill does not freeze present channels or methods of automobile distribution and would not prohibit a manufacturer from appointing an additional dealer in a community provided that the establishment of the new dealer is not a device by the manufacturer to coerce or intimidate an existing dealer. The committee emphasizes that the bill does not afford the dealer the right to be free from competition from additional franchise dealers. Appointment of added dealers in an area is a normal competitive method, for securing better distribution and curtailment of this right would be inconsistent with the antitrust objectives of this legislation. Under the bill, a manufacturer does not guarantee the dealer profitable operation or freedom from depletion of investment.

Id. at 9. Staten Island Motors, Inc. v. American Motors Sales Corp., 169 F. Supp. 378 (D. N.J. 1959), upheld the right of a manufacturer to cancel an inefficient dealer who neglected his franchise and failed to maintain a suitable outlet for the product.

486. The act's opponents have argued . . . that the inevitable consequence of the act will be "to encourage the parties to regard themselves as legal antagonists rather than as participants in a [joint] business venture" and that the climate of cooperation prevailing until the advent of the new legislation will be replaced by a "litigious atmosphere." . . . Some critics have even questioned whether the franchise system of distribution—heretofore regarded as "the approach best suited to [the] type of product and to the mutuality of interests existing between the manufacturer and dealer"—should be retained.

Kessler, Auto Dealer Franchises: Vertical Integration by Contract, 66 Yale L.J. 1135, 1177-78 (1957). (Footnotes omitted.)
problem the courts face is adjusting the conflicting interests of the dealer, manufacturer, and consuming public. If the term “coercion” is restricted to the commission of criminal or tortious acts, then the situation will remain essentially unchanged from that which existed under section 4 of the Clayton Act prior to the adoption of the Day in Court Act. Neither the public nor the dealers will secure benefit from the act. On the other hand, if the elastic term “coercion” is expanded to its widest possible sense, the automobile dealer franchise system might be converted from one of contract integration to status integration, by turning existing franchises into permanent relationships, to the detriment of the public and manufacturer. Neither extreme is likely. It is anticipated that courts will interpret “coercion” to include only the threat of or commission of acts wrongful in themselves, plus acts not wrongful as such, for example, threat of cancellation, yet which are part of an unlawful scheme or plan—specifically, a plan of violation of the spirit of the antitrust laws.

Given this interpretation of the act, not all dealers who desire legal redress for cancellation will gain it. Indeed, many, if not most, of the cancelled dealer antitrust suits would result, as before, in judgment for the defendant.

487. The public will not secure the benefits of increased competition (e.g., dual lines). For the emergence of dual and multiple franchises, see Automotive News, Sept. 2, 1958, p. 2, col. 1; id., Aug. 19, 1958, p. 58, col. 1; id., Aug. 26, 1958, p. 2, col. 1. The Justice Department has commented favorably on the practice. Address by Victor R. Hanson, [Former] Assistant Attorney General in Charge of the Antitrust Division, to Meeting of NIADA, Nov. 26, 1957. But will the practice survive the introduction of the Big Three's small cars?

For a discussion of the “threat” to franchised dealers by “supermarket” competition, see 1 Whitney, Antitrust Policies 514-15 (1958).

488. The manufacturer will, in effect, be deprived of the flexibility of contract integration, see note 479 supra, and the public will not enjoy the increased competition between manufacturers thus made possible.

489. Dealers will not, absent coercion, be protected against “arbitrary” refusals to renew. Therefore the manufacturer who waits out the expiration date of the franchise without resorting to coercion can avoid the bite of the act, at least theoretically. This may occasionally result in hardship to a terminated dealer. But the contrary position, taken in Kessler, supra note 486, at 1183 (failure to renew must be in good faith), may lead to even greater evils, as indicated in the text. Furthermore, even under the narrow interpretation of the act taken here, the juridical risk placed on the manufacturer is formidable, particularly since the line between the unlawful coercion and legitimate persuasion is very tenuous indeed. That tension should not be further increased.

The one case to have been decided on the merits to date under the act has been a victory for the manufacturer. Staten Island Motors, Inc. v. American Motors Sales Corp., 169 F. Supp. 378 (D.N.J. 1959). A cancelled dealer sought recovery for breach of contract, violation of the New York General Business Law and violation of the Day in Court Act. The dealer had been operating under one year franchise agreements until 1958 when the defendant refused to renew. The reasons given were insufficient sales, absenteeism, and lack of a suitable place for display. After ruling out the first two causes of action, the court dealt at length with the Day in Court Act. Finding that “the plain meaning of the Act indicates that the restrictions which it imposes extend only to those dealings between parties wherein coercion or intimidation or threats of the same are involved,” id. at 382, it found that the admitted facts did not indicate coercion, and it awarded summary judgment to the defend-
Hence, under this interpretation, the dealer community may feel that the act does not go far enough. Nevertheless, it is submitted that such a construction will effectuate the purposes of the act in a manner most in accordance with the intentions of Congress and the public interest. One can quarrel with the proposition that the dealer should recover damages only if by so doing he vindicates the public interest. But one should not quarrel with the proposition that the dealer should not take damages if his suit will result in injury to the public. Extending the scope of the term “coercion” beyond unlawful acts and acts which will further an anticompetitive purpose may so hamper the distribution of automobiles that the ultimate consumer will be injured, and will be forced to foot the bill for preserving inefficient means of distribution. It is submitted that this is not a social cost which should be borne by the car buyer.

Related legislation. A bill identical to the Auto Dealer Day in Court Act has been proposed for gasoline distribution. And the Senate Small Business Committee has been considering extension of the Day in Court Act to other industries which use the franchise system of retail distribution. Thus, Plaintiff had claimed that the act was violated in four ways: (1) Defendant withheld automobiles ordered by plaintiff’s son. The court held, however, that since the son lacked authority under the contract to place orders the defendant was under no obligation to supply the automobiles. (2) Defendant insisted that the 1957 agreement be signed in New Jersey rather than in Staten Island where plaintiff’s business was located. The court regarded this as a sound business practice. (3) The terms of the 1957 agreement relating to defendant’s obligations upon failure to renew were unfair. The court found, however, that plaintiff signed the agreement voluntarily and was not coerced into so doing. (4) Defendant failed to renew. The court found no coercion in the admitted facts and emphasized that a manufacturer has a right to expect the dealer to maintain a suitable outlet for his products.

A number of other cancelled dealers have filed suits under the Act claiming one or more of the following: insufficient deliveries; unfair and discriminatory distribution of popular and unpopular models; insufficient advertising in the dealer’s locality; larger discounts given to competitors, and arbitrary cancellation. Among the cases which have been filed are Jim Kelly, Inc. v. Chrysler Corp., and McClaren Motors, Inc. v. Chrysler Corp., both in Michigan, Automotive News, Nov. 24, 1958, p. 2, col. 1; B. H. Dario Co. v. General Motors, in Rhode Island, Automotive News, March 2, 1959, p. 6, col. 2; Raleigh R. Leach & Co. v. Ford Motor Co., in California, Automotive News, March 30, 1959, p. 8, col. 1; Blenke Bros. Motors, Inc. v. Chrysler Corp., and S. H. Arnolt, Inc. v. Renault, both in Illinois, Automotive News, June 22, 1959, p. 45, col. 2.


491. H.R. 425, 85th Cong., 1st Sess. (1957). This bill, like the automobile dealer act after which it is patterned, restricts its coverage to written franchise contracts. While automobile franchises are written, as a matter of business practice, franchises in other industries are often informal and oral. See Hewitt, The Furor Over Dealer Franchises, 1 Bus. Horizons 80, 82 (1958).

492. S. Rep. No. 1282, 85th Cong., 2d Sess. 47 (1958). When exclusive dealing is not anticompetitive, should “coerced” exclusivity be justified? The two senses of “coercion” distinguished, note 478 supra, must be considered separately. The unlawful
the Auto Dealer Day in Court Act may be the harbinger of extensive legislative activity in the field of contract-integrated retail distribution. Because of its potentiality for harm to the public and to industry, extension of the Day in Court Act philosophy to other areas might better be postponed until the actual effect of the act on the automobile industry becomes apparent. In this respect, future court decisions under the new act merit close attention.

Two measures closely related to the Auto Dealer Day in Court Act may have a significant effect on the operation of the new law. The Automobile Information Disclosure Act ("Sticker Act"), and various bills to legalize territorial security appear to be directed at weakening section 4 of the Day Act. Purpose aspect is irrelevant here, since we have stipulated no anticompetitive effect, and the authors deny that any purpose other than restraining trade is unlawful in this context. Hence, mere refusal to deal on nonexclusive terms ought not be considered "coercion" under a Day in Court Act when they have no effect on entry. As for the other aspect of coercion, the "vi et armis" type of intimidatory behavior forbidden by the Day in Court Act, it cannot be denied that such behavior is within the scope of Congress' regulatory powers. But should Congress legislate in this area, rather than leave it to the states? Are policy purposes served by such legislative interference with business activities? The authors incline slightly more toward federal inaction than action in this area.

493. Particularly dubious is the basic countervailing power rationale of The Day in Court Act. Countervailing power may work under the National Labor Relations Act, as amended, Labor-Management Relations Act, 61 Stat. 136 (1947), 29 U.S.C. § 151 (1952), but it is essentially foreign to the philosophy of antitrust, which prefers to decrease power at every point rather than to counterbalance it. That the consumer will benefit from the rivalry between the countervailing powers is doubtful. See DILAM & KAHN, FAIR COMPETITION 238 (1954); Adams, Competition, Monopoly and Countervailing Power, 67 Q.J. Econ. 469, 475-77 (1953); Bain, Economies of Scale, Concentration, and the Conditions of Entry in Twenty Manufacturing Industries, 44 Am. Econ. Rev. 15 (1954); Whitney, Errors in the Concept of Countervailing Power, 26 J. Bus. 238 (1953). It is perhaps more likely that the latter will join forces against the consumer; indeed, under a games theory analysis, it is irrational to expect anything but a coalition. See McKinsey, INTRODUCTION TO THE THEORY OF GAMES ch. 15 (1952).


495. The four bills presently pending are as follows:

S. 997, 86th Cong., 1st Sess. (1959), introduced by Senator Langer, R. N.D., allowing a system of territory security enforced by penalties. Under this measure, a franchise contract provision would be valid which required a dealer selling to a customer outside his territory to make an "infringement payment" to the dealer whose territory was invaded. This bill is not restricted to the automobile industry, but would extend to the distribution and sale of all "complex mechanical equipment."

S. 2042, 86th Cong., 1st Sess. (1959), introduced by Senator Schoeppel, R. Kans., similar to S. 997, but dealing exclusively with the automobile industry.

S. 2047, 86th Cong., 1st Sess. (1959), introduced by Senator Hruska, R. Neb., allowing a system of territory security in the automobile industry enforced by bonus payments. Under this measure, a franchise agreement provision would be valid which required "incentive payments" to be made by the manufacturer to the dealer each time he made a sale to a customer from within his territory.

S. 2151, 86th Cong., 1st Sess. (1959) introduced by Senator Monroney, D. Okla., similar
in Court Act, which disclaims repeal or modification of the antitrust laws. The Sticker Act, purportedly aimed at preventing dealers from misleading customers as to the “list” price of cars and accessories, requires every new car to bear a sticker listing suggested prices and listing the name and address of the auto dealer to whom the car was originally consigned. Critics of the act have contended that its real purpose is suppression of “bootlegging”—the practice of franchised dealers’ selling overstocked cars to cut-rate, unfranchised auto dealers. The latter assert that they will be deprived of their source of supply because franchised dealers will fear manufacturer retaliation. Instances have already been reported where manufacturers took to S. 2047, except that it refers to the bonus payment as an “additional discount, rebate or allowance” rather than as an “incentive payment.”

All four bills were referred to the Senate Subcommittee on Automobile Marketing Practices, and hearings commenced on June 22, 1959. Statements favorable to some form of territory security were filed with the committee by representatives of General Motors, the Department of Commerce, and the National Automobile Dealers Association (NADA), which had conducted a poll of its membership showing 59% of the 52% response favoring some form of legislation permitting territory security. Hearings on S. 997 et al. Before the Subcommittee on Automobile Marketing Practices of the Senate Committee on Interstate and Foreign Commerce, 86th Cong., 1st Sess. 19, 55, 77, 99 (1959). Unfavorable statements were filed by representatives of the National Independent Automobile Dealers Association (NIADA), the Federal Trade Commission, the Department of Justice, Studebaker-Packard Motor Co., Chrysler Motor Co. and a group of North Carolina franchised dealers who resigned from the NADA in protest over its position. Id. at 42, 123, 137, 171, 180, 189. The Ford Motor Co. and American Motor Co. took a neutral position. Id. at 176, 180. Although chances of passage are believed to be slight, the possibility has been noted that a compromise bill might emerge from the hearings permitting manufacturers and dealers to agree on territory security arrangements enforced by either bonus payments or penalties. See Automotive News, June 1, 1959, p. 1, col. 3; id. June 15, 1959, p. 1, col. 1; id. June 22, 1959, p. 1, col. 5; id. June 29, 1959, p. 1, col. 4; id. July 6, 1959, p. 1, col. 2; id. Aug. 10, 1959, p. 1, col. 5.

496. The National Independent Automobile Dealers Association (NIADA), representing imported and used car dealers, has been critical of the act in so far as it requires disclosure of the name and address of the dealer to whom the automobile was originally sold. See id. Nov. 24, 1958, p. 1, cols. 2, 4; id. Feb. 2, 1959, p. 2, col. 1.

497. Former Antitrust Division Chief, Hansen, defines “bootlegging”: This is nothing more or less than the sale by a franchised dealer to another dealer of new cars which he is unable or unwilling to sell at retail . . . . I can see no reason why this form of competition is not entitled to its test in the market place. . . . Proposed contractual provisions to be included in franchised dealer sales agreements, to avoid antitrust attack, must not have either the purpose or effect of preventing . . . [this]. Speech to National Independent Automobile Dealers Ass'n, Nov. 26, 1957, p. 8. For a description of the business operation of a successful “bootlegger,” see Automotive News, June 22, 1959, p. 1, col. 2.

498. See note 496 supra. Since this act does not attempt to amend the antitrust laws, it would appear that any manufacturer caught using information obtained from the mandatory sticker in order to prevent dealers from selling to bootleggers would be in serious antitrust difficulties. See note 500 infra and accompanying text. Nevertheless, the improved
reprisals against bootlegging dealers who were traced by means of the stickers the act requires. Thus, this piece of legislation may function as a legislative equivalent to ant/bootlegging clauses, which would probably be restraints on alienation, unlawful under the rationale of *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, and whose attempted enforcement by threat of nonrenewal or cancellation would give rise to a dealer cause of action under the Day in Court Act.

The territorial security bills propose to make it legal to insert in franchise contracts prohibitions against the practice of "cross-selling," i.e., selling to customers whose residence is in the territory allocated to another dealer. Some bills allow penalty clauses while others allow rebates or "incentive payments." The Justice Department has long opposed manufacturer efforts to include such restrictions in franchise contracts. Anti-cross-selling clauses would seem to violate the section 1 Sherman Act per se rule against allocation of territory. Thus, these two statutes appear to attempt to soften the opportunity given for extra-legal policing of dealers is obvious. According to the National Independent Automobile Dealers Association (NIADA), dealers have complained of manufacturer pressure exerted on franchised dealers who sold new cars to independent dealers. See *Automotive News*, Nov. 24, 1958, p. 1, col. 2.

499. The NIADA is presently conducting a poll to determine the impact of the Sticker Act on the monopoly of "bootlegged" cars. *Id.* May 11, 1959, p. 1, col. 5. Many franchised dealers reportedly believe that the act has "practically wiped out bootlegging." *Id.* Feb. 9, 1959, p. 1, col. 2.

500. 220 U.S. 373 (1911).

501. S. 997, 86th Cong., 1st Sess. (1959), introduced by Senator Langer, validates franchise contracts which require "infringement payment" from the cross-selling dealer to the dealer whose territory he invades. Significantly, the scope of the bill is not restricted to the automotive industry; it attempts to prevent the cross-selling of all power-operated machinery and appliances distributed under franchises. S. 2042, 86th Cong., 1st Sess. (1959), introduced by Senator Schoeppel, otherwise similar to S. 997, deals only with the automobile industry.

502. S. 2047, 86th Cong., 2d Sess. (1959), introduced by Senator Hruska, validates "incentive payments" to auto dealers on sales made within their territories. S. 2151, 86th Cong., 2d Sess. (1959), introduced by Senator Monroney, is similar to S. 2047, but uses the term "discount, rebate or allowance" in place of "incentive payment."


vigor of the antitrust laws, in retail distribution, so that those who would rather not compete may be relieved from the rigors of competition. The Franchised Dealer Bill is particularly significant because its scope is not restricted to the automobile industry. It attempts to prevent the cross-selling of all power-operated machinery and appliances distributed under franchises. If such legislation were widely adopted, competition in the retail distribution of merchandise affected might well suffer.

A Statutory Duty To Deal

A direct approach to the refusal to deal problem has been suggested by Dr. Vernon Mund in a report prepared for the Senate Small Business Committee. Legislation is proposed "requiring producers of standard products who hold themselves out as dealing with the public, and who control a substantial percentage of the output in their area of practical shipment, to sell to all comers offering to meet the terms of sale." This proposal is not unlike a section of the original Clayton Bill which passed the House in 1914 but was deleted by the Senate Committee before passage of the act. The excised section imposed a duty upon owners and transporters of hydro-electric energy, coal, oil, gas and other minerals to sell to all responsible persons. The Senate felt such a statute "would practically compel owners of the products named to sell to anyone or else decline to do so at the peril of incurring heavy penalties, [and] would project us into a field of legislation at once untried, complicated, and dangerous."

The fears which led to elimination of the refusal to deal section might be considered somewhat exaggerated, inasmuch as innkeepers, common carriers, and public utilities are able to exist under such a regime without being harassed by strike suits. Nevertheless the proposed legislation is quite drastic and it may lead to undesirable and unexpected results. A blanket condemnation of refusals to deal, without limitation to those situations where there is a monopoly or where refusal to deal is used to accomplish an improper

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506. Id. at 92, 102. Dr. Mund also would like to have the franchise contract, like the insurance contract, made by legislature and supervised and rewritten by FTC. Id. at 96, 103. A similar proposal may be found in the Ground Rules Bill, S. 3946, 84th Cong., 2d Sess. (1956). For a discussion of the Justice Department's criticism of the latter bill, see Hearings on Automobile Marketing Practices Before a Subcommittee of the Senate Committee on Interstate and Foreign Commerce, 84th Cong., 2d Sess., pt. 2, at 1489-98 (1956).

507. H.R. 15657, 63d Cong., 2d Sess. § 3 (1914).


510. See Lorain Journal Co. v. United States, 343 U.S. 143 (1951); Eastman Kodak
VERTICAL INTEGRATION

purpose—e.g., price fixing or coercion of exclusivity—covers too much ground. It is perhaps difficult to imagine an innkeeper with a legitimate motive to violate his duty to deal with "all comers offering to meet the terms of sale" or with any "responsible person." But in the ordinary business context, one can imagine many circumstances in which it is perfectly proper for a man to refuse to deal with another without being called to an accounting before a court or commission and being exposed to the attendant juridical risks. Thus, other alternatives should be explored before resorting to so sweeping an enactment. It is submitted that if any changes in the antitrust laws are to be made, these changes should be limited to the most immediate problem—elimination of barriers to entry erected by exclusive dealing—whether exclusivity is achieved by express agreement or by indirection.511

Amendments to the Clayton Act

Perhaps amendment of the Clayton Act can solve the problem. Section 3 could be amended to include offers and attempts to sell on exclusive dealing conditions. This solution would not be satisfactory, however, because it could be evaded by very careful behavior, just as coercion can be avoided under the Auto Dealer Franchise Act by circumspection. Moreover, the same proximate cause problem as presently exists under section 4 would survive—the attempt or offer would not itself be the proximate cause of an injury.

A more effective solution would focus violation upon the refusal to deal rather than the offer to deal on exclusive terms. Thus, Congress could declare it "unlawful to refuse to deal with a person for the reason that he deals or proposes to deal in the goods of a competitor of the prospective seller where the effect of the practice may be to lessen competition substantially or tend to create a monopoly." Such a statutory change would overcome the consummated sale and the proximate cause hurdles, but another serious obstacle would still remain—the damages problem. The courts should be free to award an injured plaintiff the value of the cancelled dealership. But would not expectation damages, if claimed, be considered too re-

511. The only justification for a duty to deal is that refusal to deal may harm the public. Therefore, there should be no duty to deal if competition will continue to flourish because close substitute products are amply available to the consumer.

512. "Refusal to deal" is intended to include "cancellation" and "termination," under the rule of Hudson Sales Corp. v. Waldrip, 211 F.2d 268 (5th Cir.), cert. denied, 348 U.S. 821 (1954).


mote and speculative? The existing cases are divided as to whether “lost profits” are recoverable in cancelled dealership actions.519 This difficulty might be remedied by adding to section 4 of the Clayton Act a provision that courts include in damages the value of reasonable expectation interests.514 Perhaps the most economical procedure would be to amend section 4 as follows:

Sec. 4C. Any person injured because he refuses to accede to a proposed agreement or understanding for exclusive dealing which would, if consummated, violate the antitrust laws, has a cause of action under § 4 of the Clayton Act. Injury may include damage to reasonable expectation interests.

This formulation attempts to overcome the unduly technical interpretation of present section 4 of the Clayton Act. It seeks to bring private antitrust law into harmony with public antitrust law. At the same time, established business patterns and freedom of contract are restricted only to the extent that they come in conflict with basic antitrust principles. The term “exclusive dealing” is used in place of “sale,” and no limitation as to “goods” is used, to avoid the problems under present section 3 with respect to noncommodities or purchases. The authors advance this proposed amendment to section 4 as the means most to be preferred for solution of the refusal to deal problem.

III. VERTICAL INTEGRATION AND REGULATION OF PRICING

The Vulnerability of Contract

In addition to the antitrust laws, the laws regulating pricing significantly affect ownership and contract as vertical integration devices. The form of integration adopted—contract or ownership—may vary considerably the impact of such legislation on the integrated firms. For example, the principal statute—section 2 of the Robinson-Patman Act, which forbids price discrimination515—is applicable only to contractual relationships.

In part I, the economic advantages to seller and buyer under a contract integration system were discussed. When each party keeps his savings to himself, and does not attempt to share them with the other, there is no Robinson-Patman problem. Should the seller, however, to make integration worth the buyer’s while, attempt to share his savings with the buyer in the form of a price discount, there may be a violation of the act.516

513. The cases are discussed in Kessler, supra note 486, at 1185-88.
514. For discussion of the appropriate measure of damages in these cases, see id. at 1187-89.
516. This might occur in a situation where integration offered far more benefit to the seller than the buyer.
The Robinson-Patman Act

Section 2(a) of the Robinson-Patman Act bans "price discrimination" with respect to like commodities by a seller between his buyers. The ban is not imposed, however, when the price differential is cost-justified, reflects good faith meeting of competition, reflects a change in "marketability" conditions, or when there is no lessening of competition or injury to competitors. As between vertical integration by contract and buying in the spot market these qualifications seem to prefer contract integration. But the advantages turn out, in large measure, to be nonexistent.

Defenses Under the Act

Cost Justification. Any defense based on cost justification is probably doomed. The Report of the Attorney General's Committee, speaking of cost justification in general, pointed out that "the cost defense has proved largely illusory in practice." And in the language of the Supreme Court, "proof

517. There can be Robinson-Patman discrimination only when the seller sells to two or more buyers. If the seller's entire output is sold to one buyer, no price differential can exist. Hence, the discussion which follows is directed only to the plural buyer situation. Moreover, discriminatory purchasing is not within the scope of the Robinson-Patman Act; like Clayton Act § 3, the Robinson-Patman Act is not directed against buying. 81 Cong. Rec. 2340 (1937) (informal opinion of FTC). However, both the Sherman Act and § 5 of the FTC Act are applicable here. See ATT'Y GEN. NAT'L COMM. ANTITRUST REP. 164 n.116, 201 n.230 (1955) ; notes 276-77 supra. Thus, in MPAS, had respondent not obtained output contracts but relied on contracts providing a higher payment conditioned on exclusive dealing, it is doubtful that the outcome would have been different. To date there is no case law on this point.

518. A defense based on lack of a substantial lessening of competition would probably be unsuccessful, since the act is also applicable when competition with the buyer or seller may be injured, destroyed or prevented. Thus, violation of the act is not dependent on a showing of injury to competition; injury to competitors suffices. E. Edelman & Co. v. FTC, 239 F.2d 152, 155 (7th Cir. 1956), cert. denied, 355 U.S. 941 (1958) (individual competitive situations rather than competition in general). Compare ATT'Y GEN. NAT'L COMM. ANTITRUST REP. 165 n.120, 166 n.121 (1955). And injury to competitors follows almost automatically from the existence of the differential. Rowe, Price Differentials and Product Differentiation, 66 YALE L.J. 1, 18-21 (1956). The leading case on this point is Samuel H. Moss, Inc. v. FTC, 148 F.2d 378 (2d Cir. 1945). In that case the Second Circuit read § 2(b) of the Robinson-Patman Act to place the burden of proof of lack of injury on the seller who sets two prices. See also FTC v. Morton Salt Co., 334 U.S. 37 (1948) ; FTC v. Standard Brands, Inc., 189 F.2d 510 (2d Cir. 1951) ; Note, 66 YALE L.J. 935 n.2 (1957) (collecting cases). The Attorney-General's Report takes a more sanguine but perhaps less persuasive view of the case law. ATT'Y GEN. NAT'L COMM. ANTITRUST REP. 161-63, 166 (1955) (dissent).

Note that both buyer and seller may be in violation of the act. Section 2(f) is directed specifically at buyers. Moreover, there may be a § 1 Sherman Act or § 5 FTC Act violation. FTC v. Cement Institute, 333 U.S. 683, 708 (1948) ; Triangle Conduit & Cable Co. v. FTC, 168 F.2d 175, 180 (7th Cir. 1948), aff'd per curiam by an equally divided Court sub nom. Clayton Mark & Co. v. FTC, 336 U.S. 956 (1949) ; see note 517 supra.

of a cost justification being what it is, too often no one can ascertain whether a price is cost-justified.\textsuperscript{520} These difficulties become even more formidable when the cost defense is based on economies resulting from vertical integration by contract.\textsuperscript{521} “Reliability of an adequate supply is not usually an objective fact or a calculable cost.”\textsuperscript{522} Even if existence of savings could be established, the proper allocation of the joint costs involved for Robinson-Patman Act purposes is extremely difficult.\textsuperscript{523} Finally, cost accounting is expensive.\textsuperscript{524}

Unlike Commodities. A defense might be based on a denial that the same goods are sold to the nonintegrated buyer as are sold to the contract-integrated buyer. Unless the goods sold at different prices to different buyers are of like grade and quality, the statute is inapplicable.\textsuperscript{525} This defense would point to the economic realities of the term requirements contract situation: what the contract-integrated buyer buys is not the same thing the spot market buyer buys. The integrated buyer and seller may each acquire price hedges; they secure stability of operations and shift or lessen other commercial risks. The considerations exchanged are more complex than in the simple spot sale. For these reasons, it could be argued, the spot transaction and the requirements contract transaction cannot reasonably be assimilated and be considered to involve the same type of goods.

Nevertheless, however plausible the foregoing defense, and in the opinion of the authors it is a meritorious one, it is unlikely that it will be successful.\textsuperscript{526} The view may be taken that any cost justification situation also involves a “like” commodity problem. Gasoline delivered to the dealer is not the same commodity as gasoline picked up at the tank car, nor

\begin{footnotesize}
\begin{enumerate}
\item[520.] Automatic Canteen Co. of America v. FTC, 346 U.S. 61, 79 (1953).
\item[522.] Adelman, Integration and Antitrust Policy, 63 Harv. L. Rev. 27, 29 (1949).
\item[523.] Hale & Hale, Market Power: Size and Shape Under the Sherman Act 227-29 (1958); see Adelman, supra note 522, at 30-31.
\item[526.] This defense was raised in Goodyear Tire & Rubber Co., 22 F.T.C. 232 (1936). Goodyear sold Sears its “Allstate” tires requirements on a cost plus 6% basis, “Allstate” being the private brand of Sears. This price was substantially lower than the price of Goodyear brand tires to retailers. Goodyear unsuccessfully argued, \textit{inter alia}, that the Sears assured volume insured stability by leveling production (thereby securing to Goodyear reduced overhead) and eliminated raw material price fluctuation hazards and credit losses. This, together with the absence of advertising expenses on “Allstate” tires, allegedly made the “Allstate” brand and Goodyear brand transactions two separate businesses in which Goodyear was engaged. The FTC held that “the alleged hazards and other similar factors
\end{enumerate}
\end{footnotesize}
is nationally advertised brand aspirin the same commodity, marketwise, as nonbrand aspirin. But neither court nor FTC is likely to hold that a producer of these commodities may charge different prices for them, absent cost justification of the price differential.\textsuperscript{527} Hence it is probable that a court will be impelled by similar reasoning to require that cost justification actually be established in a contract integration case, rather than permit the integration arrangement to escape the operation of the act completely via the like quality requirement. And until section 2(a) is reinterpreted by the courts or revised by the legislature,\textsuperscript{528} such cost justification attempts will prove practically hopeless a task. Furthermore, making substantially equivalent contract integration and price discount arrangements available to all customers will probably afford no defense to charges under the statute.\textsuperscript{529}

\textit{Term Contract Prices}

The preceding analysis has been directed to the situation where the seller attempts to share with the buyer the benefits of the contract integration relationship. Even in the absence of such attempts, some risk of Robinson-
Patman Act violation remains. The price terms in a requirements contract may provide for a fixed price over the term, a price formula based on the spot market price, or a cost-plus-price formula. Each of these price terms might be adjudged discriminatory, if it is used to give the buyer a non-cost-justified advantage, so as to induce him to enter into the contract.

Other Price Discrimination Laws

Two further pricing regulation statutes may raise problems for contract vertical integration—section 3 of the Robinson-Patman Act and section 3 of the Clayton Act. Section 3 of the Robinson-Patman Act, a purely criminal statute, prohibits (a) being a party to a sale which discriminates against competitors of the buyer, when goods of like grade and quantity are involved, (b) seller price discrimination aimed at destroying competition or eliminating a competitor, or (c) selling at an unreasonably low price to destroy

530. For a more elaborate catalogue of flexible price terms, see Horowitz, Robinson-Patman Act Aspects of Long-Term Contracts, 28 So. Cal. L. Rev. 280, 281 (1953).

531. When a price rise is imminent, offering favored buyers the opportunity to make futures purchases at current prices is a violation. Corn Prods. Ref. Co. v. FTC, 324 U.S. 726, 739-40 (1945); see Van Camp Sea Food Co., 46 F.T.C. 1087 (1949) (dismissed upon discontinuance by respondent of acts complained against, inter alia, selling futures at prices under current spot market prices to favored buyers). But when there is no attempt to favor certain customers, and the opportunity to make futures purchases at the same price is open to all, there is legislative history suggesting that no violation will occur. 1 TRADE Reg. Rep. ¶ 3305.671; Hearings Before House Committee on the Judiciary, 74th Cong., 1st Sess., ser. 10, at 24 (1935):

There is a price discrimination at the time of delivery.... But the point is the futures purchaser has committed himself at a different time, under different market conditions; he has taken a different element of risk. There is nothing in the bill to prevent freedom in buying and selling on a basis of the seasonal differential on varieties.... The conditions affecting the two transactions would be the result of market conditions which obviously would be different. But if a manufacturer said to chain A, “I will give you a December future at $2 a case,” and said to independent B at the same time, comparably, “You are going to have to pay $2.50 a case for December futures,” that would be a discrimination.

(Statement of Mr. Teegarden.) Nevertheless, the analogy between futures sales and a term requirement contract is incomplete, and that the FTC and courts will refuse to believe that risk of price fluctuations is an economic cost which must be paid for is quite possible.

Still another possible defense might be the changing market conditions proviso of § 2(a). The defense might be that this proviso justifies the lower prices to the long-term buyers or the raised prices to the spot buyers. See Horowitz, Robinson-Patman Act Aspects of Long-Term Contracts, 28 So. Cal. L. Rev. 280, 295 n.42 (1955). The validity of this defense is most dubious. Ordinary market changes would hardly appear to be ejusdem generis with the type of changes given in § 2(a) as examples within the proviso—inminent deterioration, seasonal obsolescence, distress sale by court order, and discontinuance of the business. But see ATT'y GEN. NAT'L COMM. ANTITRUST REP. 178-79 (1955).

competition or eliminate a competitor. This statute would not appear to present serious difficulties to the contract integrator because the Justice Department has chosen not to enforce it.\(^{533}\) Moreover, its prohibitions are probably inapplicable to the ordinary vertical integration by contract situation. The subsection (a) requirement of like quantity is unlikely to be satisfied when an integration relationship is compared with a spot market buyer-seller relationship. Furthermore, violation of subsections (b) and (c) requires that the seller intend to destroy competition or eliminate a competitor, purposes foreign to most vertical integration situations.

Section 3 of the Clayton Act includes a clause forbidding fixing a price for goods or granting a discount or rebate on condition, agreement, or understanding that the buyer's requirements be bought from the seller, where there may be substantial lessening of competition or tendency to create a monopoly. Why Congress added this prohibition to its blanket condemnation of requirements contracts which may substantially lessen competition or tend to create a monopoly is unclear.\(^{534}\) Perhaps what Congress intended was to reach the contract which does not bind the buyer to purchase his entire requirements from the seller, but which offers him a lower price provided that he does. That is, Congress was not attempting to pass an additional price discrimination law, but was rather attempting to plug up a potential loophole in its exclusive dealing law. This would account for the use of "discount" rather than "discrimination" in the wording.\(^{535}\) It would seem, however, that under the theory of the Richfield case,\(^{536}\) such a contract would constitute an understanding that the buyer not deal with competitors of the seller. In any case it would appear that this clause of section 3 of the Clayton Act poses no greater obstacle to vertical integration by contract than does the rest of section 3. Finally, it is doubtful that the exculatory provisions of Robinson-Patman Act section 2—cost-justification, good-faith meeting of competition, change in marketability—would be read into either section 3 by the courts.\(^{537}\)

\(^{533}\) Nashville Milk Co. v. Carnation Co., \textit{supra} note 532, at 387-88 (dissenting opinion); ATT'Y GEN. NAT'L COMM. ANTITRUST REP. 199 (1955). Moreover, there are serious doubts as to the constitutionality of the statute. \textit{Id.} at 200 (vagueness).

\(^{534}\) If the price regulation clause of § 3 is aimed merely at explicit requirement contracts which specify a price for the goods sold or which grant a price concession, then it adds nothing to the other clause of § 3. The price clause could have additional vertical integration implications if "substantially lessen competition" carries a different significance in this context from its ordinary § 3 significance, but that courts will so interpret the law is extremely doubtful in view of their assimilation, in the vertical integration context, of § 7 "substantially lessen competition" to § 3 "substantially lessen competition." See discussion of \textit{du Pont} case, \textit{supra} at notes 297-307 for analysis of § 3-§ 7 coalescence.

\(^{535}\) Moreover, "discount" under § 3 is unlike "discrimination" under § 2(a) in that no plurality of buyers would appear to be required. See note 517 \textit{supra}.

\(^{536}\) See text at notes 166-71 \textit{supra}.

\(^{537}\) See ATT'Y GEN. NAT'L COMM. ANTITRUST REP. 199 (1955). \textit{But see id.} at 200 & n.229. In Horlicks Corp., 47 F.T.C. 169, 174-75 (1930), the Commission found a § 3 Clay-
In summary, it appears that, with respect to pricing regulation, vertical integration by contract is less advantageous than ownership integration. Price discrimination laws pose hazards to even the bona fide contract integrator. These hazards can be minimized, however, by the adoption of appropriate price terms in the contract, for example, market price on delivery. In any case, the requirements contract buyer would be well advised to settle for the economic advantages of the integration relationship itself in the operation of his business, rather than press for price concessions as well; by the same token, the seller seeking to integrate buyers by contract should confine his economic persuasion to pointing out the mutual benefits available to each party in the operation of his own business.

**Ownership Integration as an Avoidance Device**

Ownership integration may prove to be of great value to the firm deliberately seeking to evade the Robinson-Patman Act or price regulation.\(^5\) Because contract, whether in the spot market or under term agreements, necessarily involves sales, it can be subject to this type of legislation. On the other hand, whenever the comparative technological advantages of contract as against ownership, or even of integration over nonintegration, are relatively unimportant, and when the primary goal of the firm is maximization of its revenues in the face of regulatory legislation, then contract is at a decided disadvantage to vertical integration by ownership.

**Discrimination**

When a differentiated market exists, it is possible for a monopolist to maximize his profits by charging different prices in the different markets.\(^6\) For

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\(^5\) Of course, whether such "evasion" is socially desirable does not depend only on the respective social or economic merits of contract integration as contrasted with ownership integration, but also on one's evaluation of the philosophy and merits of these laws. This Article does not attempt to give such an evaluation. This section of this study seeks to analyze the law as it is rather than prescribe what the law should be. For penetrating analyses of the merits of the Robinson-Patman Act and its consistency with the overall goals of the antitrust laws, see Adelman, *The Consistency of the Robinson-Patman Act*, 6 STAN. L. REV. 3 (1953) ("economic analysis only"); Rowe, *Price Discrimination, Competition, and Confusion: Another Look at Robinson-Patman*, 60 YALE L.J. 929 (1951); Simon, *The Fantasy of the Phrase "Injury to Competition, 15 LAW & CONTEMP. PROB. 258 (1950); ATT'Y GEN. NAT'L COMM. ANTITRUST REP. 155-221 (1955). See also Rowe, Price Differentials and Product Differentiation: The Issues Under the Robinson-Patman Act, 66 YALE L.J. 1, 34 n.141 (1956) (collecting authorities); Patman, *For H.R. 11 and S. 11*, 11 VAND. L. REV. 399 (1958) ; Comment, 53 NW. U.L. REV. 253 (1959).

\(^6\) Boulding, *Economic Analysis* 608, 611-12 (3d ed. 1955); Stigler, *The Theory of Price* 214-18 (rev. ed. 1952) (differentiated markets are those separated from one another by time, space, or distribution methods); see id. at 214.
purposes of analysis, let us assume that a monopoly of aluminum production exists. In order to compete with copper for transmission line cable, the price of aluminum must be lower than its price when it competes with steel for aircraft structural use. The reason for this is the comparative substitutibility of the competitive materials in the former market and the lack of substitutability in the latter; copper can readily be substituted for aluminum in cable, but steel cannot readily replace aluminum in aircraft manufacture. Charging lower prices to cable makers than to airplane makers would maximize the aluminum company's revenue. Two great obstacles exist, however, to such a maximization scheme: (1) arbitrage between markets, and (2) the Robinson-Patman Act, which forbids price discrimination.

Arbitrage, the movement of low-priced aluminum from the cable market to the higher price aircraft market, would defeat the profit maximization plans of the aluminum company because aircraft users would, out of "a primitive aversion to buying at a higher price when a lower price is available," buy their aluminum from cable fabricators willing to resell to them.\footnote{540} Moreover, charging different prices to different users may subject the aluminum company to the penalties of the Robinson-Patman Act, because the discrimination will injure the "competition" by copper as a cable material.\footnote{541} Forward

540. \textit{Id. at 215-16;} \textit{Boulding, op. cit. supra} note 539, at 608, 613-14.


The "good faith meeting of competition" defense of Robinson-Patman § 2(b) is probably unavailable in the hypothetical case in the text because there is a system of consistent price difference between markets, instead of "sporadic" price cutting to combat "raids." See \textit{FTC v. National Lead Co.}, 352 U.S. 419, 431 (1957); \textit{FTC v. Cement Institute}, 333 U.S. 683, 725 (1948); \textit{FTC v. A. E. Staley Mfg. Co.}, 324 U.S. 746 (1945). \textit{But see Att'y Gen. Nat'l Comm. Antitrust Rep. 182} (1955). The good faith defense is also probably un-
vertical integration through ownership eliminates both these obstacles. When
a cable plant vertically integrated by ownership is set up, no unwanted
arbitrage can occur, and no unlawful price discrimination is apparent.

Available if there is an intent to destroy competition or eliminate a competitor (cf. Robinson-Patman § 3). The fact that copper is the historical transmission cable material and aluminum the "interloper" would probably lead a court or the FTC to the conclusion that aluminum is trying to eliminate copper as a competitor. Moreover, it is unlikely that there can be good faith meeting of competition when one tries to capture a new market by discriminatory pricing. Standard Oil Co. v. FTC, 340 U.S. 231, 249-50 (1951); Standard Motor Prods., Inc. v. FTC, 265 F.2d 674, 677 (2d Cir. 1959); see Moore v. Mead's Fine Bread Co., 348 U.S. 115 (1954). But see Balian Ice Cream Co. v. Arden Farms Co., 104 F. Supp. 796 (S.D. Cal. 1952), aff'd, 231 F.2d 356 (9th Cir. 1956), cert. denied, 350 U.S. 991 (1956); Levy, How To Meet Price Competition, in How To Comply With The Robinson-Patman Act 103, 108 (CCH 1957). The Balian case has been strongly criticized by the FTC. Hearings To Amend Section 2 of the Clayton Act Before the Subcommittee on Antitrust and Monopoly of the Senate Judiciary Committee, 84th Cong., 2d Sess. 227-28 (1956). The FTC has even taken the position that there cannot be good faith meeting of competition when "injury to competition" (i.e., injury to competitors) occurs. Standard Oil Co. v. FTC, 340 U.S. 231, 238-39 (1951). The bills, inter alia, S. 11, S. 315, H.R. 11, H.R. 384, H.R. 927, H.R. 2788, 86th Cong., 1st Sess., propose to reverse the Supreme Court's reversal of the FTC on this point.

542. See United States v. Aluminum Co. of America, 148 F.2d 416, 436-38 (2d Cir. 1945), from which the illustration in text is taken. The merger in United States v. Columbia Steel Co., 334 U.S. 495 (1948), may reveal an analogous attempt at geographical price discrimination by means of vertical integration: U.S. Steel (in Utah) wished to secure Consolidated (in Los Angeles) as a customer. Id. at 506. It probably was willing to meet the steel price offered by Kaiser's California plant, even though the greater distance of U.S. Steel from Consolidated would entail freight absorption. However, at that time it appeared that uniform FOB mill pricing ("uniform mill net") was compulsory. See Corn Prods. Ref. Co. v. FTC, 324 U.S. 726, 736-39 (1945); FTC v. Cement Institute, 333 U.S. 683, 721-26 (1948); Triangle Conduit & Cable Co. v. FTC, 168 F.2d 175, 179-80 (7th Cir. 1948), aff'd per curiam by an equally divided Court sub nom. Clayton Mark & Co. v. FTC, 336 U.S. 956 (1949). Vertical integration by ownership made it possible to gain the customer without risk of prosecution for receiving a higher "mill-net" from sales made to buyers in San Francisco or Seattle.

Such behavior is rational, to be sure, only in an industry where price substantially exceeds marginal cost, and is not to be expected in highly competitive industries. Absent an ample profit margin on steel, the "discrimination" would be irrational. See generally Comment, 65 Yale L.J. 34, 76-79 (1955). Compare Att'y Gen. Nat'l Comm. Antitrust Rep. 334-35 (1955). Moreover, the plan results in the extension of the first monopoly to a second level. In the example used, since the open market price the aluminum company sets for ingot is so high that aluminum cable makers could not compete with copper cable makers, no outsiders will be able to enter the aluminum cable market. The second monopoly may be unwanted, but it is unavoidable if the discrimination plan is to succeed.

543. On the company books the price "charged" the wholly owned cable maker is the price charged the sheet rollers. See Bork, Vertical Integration and the Sherman Act: The Legal History of An Economic Misconception, 22 U. Chi. L. Rev. 157, 197 (1954); Comment, 19 U. Chi. L. Rev. 583, 613-14 (1952). However, a "squeeze" might be alleged by independent aluminum cable makers, i.e., it could be claimed that the price differential which the aluminum company maintains between ingot and cable is too small to cover the cost of fabricating cable. See Jarrett v. Pittsburgh Plate Glass Co., 131 F.2d 674, 676 (5th Cir. 1942).
Price Controls

Price controls affecting some levels of production or distribution can be evaded through vertical integration by ownership when the integrated enterprise includes levels which are not under price control. For example, consider an industry where statute prevents raising prices of raw or semifinished materials. If price in the finished goods market is determined only by supply and demand, then ownership of the fabrication level may make it possible to secure some of the profit which would naturally be available in a scarcity situation. Or, in a regulated industry where the retail profit margin is fixed, control of an earlier stage of production may make it possible to inflate the cost base—for bookkeeping purposes only, of course—on which the fixed profit margin is taken and thereby make it possible to enjoy the benefits of the later stage monopoly at the earlier stage.

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1942); Baush Mach. Tool Co. v. Aluminum Co. of America, 72 F.2d 236 (2d Cir. 1934), cert. denied, 293 U.S. 589 (1934); United States v. Corn Prods. Ref. Co., 234 Fed. 964, 982-85, 1007-08 (S.D.N.Y. 1916); Hearings Before the Subcommittee on Study of Monopoly Power of the House Committee on the Judiciary, 81st Cong., 2d Sess., ser. 14, pt. 6, at 310-11, 331, 333, 334, 345, 615-16 (1950). See also cases discussed in text at notes 310-34 supra. The “squeeze” and recoupment are thoroughly discussed and discounted as fallacies in Hale & Hale, Market Power: Size and Shape Under the Sherman Act 223-27 (1958); Hale, Vertical Integration, 49 COLUM. L. REV. 921, 937-46 (1949); Bork, supra at 164-65, 182-84, 198-200. These studies show that, in a rational business order, vertical integration will not be adopted in order to carry out such practices. Of course, that “squeeze” is an economic fallacy does not mean that it will not occur in an irrational context. See Fulda, Food Distribution in the United States, The Struggle Between Independents and Chains, 99 U. PA. L. Rev. 1051, 1153-59 (1951). Query: Could A & P’s practices described by Fulda reflect, attempts, albeit unsuccessful, to create barriers to entry by use of discrimination, i.e., imposing high costs on newcomers to discourage them from entering the market? See text at notes 64-77 supra. See also Kahn, Discrimination as a Barrier to Entry: The Spark Plug Litigation, June 1959 (unpublished study in Yale Law School Library). And should it occur, could an antitrust violation be found under Sherman Act §§ 1-2, FTC Act § 5, or Robinson-Patman Act § 3?


545. McKee, The Regulation of Natural Gas 16-17 (1957); Sheahan, Integration and Exclusion in the Telephone Equipment Industry, 70 Q.J. Econ. 249, 251 (1956); Adelman, supra note 522, at 43-44; see United States v. Yellow Cab Co., 332 U.S. 218, 224-25 (1947); Smith v. Illinois Bld Tel. Co., 282 U.S. 133, 152-53 (1930); Cole, supra note 544. See also Adelman, supra note 522, at 51; Bowman, Tying Arrangements and the Leverage Problem, 67 YALE L.J. 19, 21-23 (1957) (analogous tie-in situation). Para-
On an overall evaluation, the more favorable position of ownership integration under pricing laws does not dictate the rejection of contract integration. It is submitted that the considerations discussed in part I of this Article are much more important in deciding whether to integrate by ownership or contract. Scale of operation is particularly significant in this connection.

It is hardly reasonable, for example, to suppose that concern over the Robinson-Patman Act would be the predominant factor urging a department store to purchase a textile mill. On the other hand, when the department store considers purchase of a costume jewelry manufacturer, the Robinson-Patman factor might exert greater influence. Moreover, the adoption of ownership may merely push the problem to a different level: even the most thoroughly integrated firm is not as self-sufficient as Robinson Crusoe; it must do some buying.

Desire to escape the operation of the Robinson-Patman doxically, price regulation may occasionally force a utility to divest itself of ownership-integrated sources of supply. Thus, Federal Power Commission regulation of the price that integrated pipelines could charge themselves for natural gas caused them to switch to contract integration because the price level the FPC set was below the going market rate. McKee, op. cit. supra at 18.

By the same token, taxable profits at one level of production or distribution can be avoided by siphoning them off at another, nontaxable level. See Price v. Standard Oil Co., 55 N.Y.S.2d 890, 894-95 (Sup. Ct. 1945), settlement noted and judgment modified, 273 App. Div. 890, 77 N.Y.S.2d 686 (1948) (avoidance of Venezuelan Government oil royalties based on net profits of drilling subsidiary of Standard); Magill, Allocation of Income by Corporate Contract, 44 Harv. L. Rev. 935 (1931) (avoidance of state income taxes by corporations doing business in several states).

There is an outstanding exception to this conclusion: the case of ownership backward integration into wholesaling by retailers. Discussion of this problem is omitted from this study because of its relative lack of importance in the general industrial context considered here and because of the able treatment it has received elsewhere in the legal literature. See Adelman, The Consistency of the Robinson-Patman Act, 6 Stan. L. Rev. 3 (1953); Adelman, Corporate Integration, in How To COMPLY WITH THE ANTITRUST LAWS 290, 294-96 (Van Cise & Dunn ed. 1954). See also Att'y Gen. Nat'l Comm. Antitrust Rep. 188-89, 207-09 (1955).

Moreover, with regard to resale price maintenance, an area where the philosophies of the Sherman Act and Fair Trade Laws conflict, tapered vertical integration (i.e., the use of both contract and ownership integration) is at a disadvantage with purely contractual arrangements. United States v. McKesson & Robbins, Inc., 351 U.S. 305 (1956) (resale price maintenance in tapered integration context, held price-fixing); see Note, 64 Yale L.J. 426 (1955).

On the other hand, for a monopolist, any resale price maintenance contracts are illegal. Eastman Kodak Co. v. FTC, 158 F.2d 592 (2d Cir. 1946), cert. denied, 330 U.S. 828 (1947). However, the Robinson-Patman Act problems encountered on the new level toward which the hypothetical industrialist integrates by ownership might prove less serious than those he formerly faced. Thus, Professor Adelman suggests that denial of functional discounts to A & P gives A & P an incentive to integrate backward to the manufacturing (i.e., canning) level. Adelman, Corporate Integration, supra note 546, at 298. Perhaps, A & P would be less likely to get into Robinson-Patman Act difficulties as a canner (i.e., purchaser of cans) than as a canned goods purchaser, but this is questionable.
Act in occasional situations may add impetus toward a merger decision, but it is unlikely that ownership integration can or does serve as an escape hatch from all the problems this act poses for contract vertical integration.

APPENDIX


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 . . . .


Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a misdemeanor, and, on conviction thereof, shall be punished by fine not exceeding fifty thousand dollars, or by imprisonment not exceeding one year, or by both said punishments, in the discretion of the court.


It shall be unlawful for any person engaged in commerce, in the course of such commerce, to lease or make a sale or contract for sale of goods, wares, merchandise, machinery, supplies, or other commodities, whether patented or unpatented, for use, consumption, or resale within the United States or any Territory thereof or the District of Columbia or any insular possession or other place under the jurisdiction of the United States, or fix a price charged therefor, or discount from, or rebate upon, such price, on the condition, agreement or understanding that the lessee or purchaser thereof shall not use or deal in the goods, wares, merchandise, machinery, supplies, or other commodities of a competitor or competitors of the lessor or seller, where the effect of such lease, sale, or contract for sale or such condition, agreement, or understanding may be to substantially lessen competition or tend to create a monopoly in any line of commerce.


Any person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue therefor in any district court of the United States in the district in which the defendant resides or is found or has an agent, without respect to the amount in controversy, and shall recover threefold the damages by him sustained, and the cost of suit, including a reasonable attorney's fee.


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

No corporation shall acquire, directly or indirectly, the whole or any part of the stock or other share capital and no corporation subject to the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets of one or more corporations engaged in commerce, where in any line of 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 monopoly.

This section shall not apply to corporations purchasing such stock solely for invest-
ment and not using the same by voting or otherwise to bring about, or in attempting
to bring about, the substantial lessening of competition. Nor shall anything contained
in this section prevent a corporation engaged in commerce from causing the formation
of subsidiary corporations for the actual carrying on of their immediate lawful business,
or the natural and legitimate branches or extensions thereof, or from owning and holding
all or a part of the stock of such subsidiary corporations, when the effect of such for-
mation is not to substantially lessen competition.

45 (1958):

(1) Unfair methods of competition in commerce, and unfair or deceptive acts or
practices in commerce are declared unlawful.


(a) It shall be unlawful for any person engaged in commerce, in the course of
such commerce, either directly or indirectly, to discriminate in price between different
purchasers of commodities of like grade and quality, where either or any of the purchases
involved in such discrimination are in commerce, where such commodities are sold for
use, consumption, or resale within the United States or any Territory thereof or the
District of Columbia or any insular possession or other place under the jurisdiction of
the United States, and where the effect of such discrimination may be substantially to
lessen competition or tend to create a monopoly in any line of commerce, or to injure,
destroy, or prevent competition with any person who either grants or knowingly receives
the benefit of such discrimination, or with customers of either of them: Provided, That
nothing herein contained shall prevent differentials which make only due allowance for
differences in the cost of manufacture, sale, or delivery resulting from the differing
methods or quantities in which such commodities are to such purchasers sold or delivered:
Provided, however, That the Federal Trade Commission may, after due investigation
and hearing to all interested parties, fix and establish quantity limits, and revise the
same as it finds necessary, as to particular commodities or classes of commodities, where
it finds that available purchasers in greater quantities are so few as to render differ-
entials on account thereof unreasonably discriminatory or promotive of monopoly in any
line of commerce; and the foregoing shall then not be construed to permit differentials
based on differences in quantities greater than those so fixed and established: And
provided further, That nothing herein contained shall prevent persons engaged in
selling goods, wares, or merchandise in commerce from selecting their own customers
in bona fide transactions and not in restraint of trade: And provided further, That noth-
ing herein contained shall prevent price changes from time to time where in response to
changing conditions affecting the market for or the marketability of the goods concerned,
such as but not limited to actual or imminent deterioration of perishable goods, obso-
lescence of seasonal goods, distress sales under court process, or sales in good faith
in discontinuance of business in the good concerned.

(b) Upon proof being made, at any hearing on a complaint under this section, that
there has been discrimination in price or services or facilities furnished, the burden of
rebutting the prima-facie case thus made by showing justification shall be upon the
person charged with a violation of this section, and unless justification shall be affirmatively
shown, the Commission is authorized to issue an order terminating the discrimination:
Provided, however, That nothing herein contained shall prevent a seller rebutting the
prima-facie case thus made by showing that his lower price or the furnishing of services or facilities to any purchaser was made in good faith to meet an equally low price of a competitor or the services or facilities furnished by a competitor.


It shall be unlawful for any person engaged in commerce, in the course of such commerce, to be a party to, or assist in, any transaction of sale, or contract to sell, which discriminates to his knowledge against competitors of the purchaser, in that, any discount, rebate, allowance, or advertising service charge is granted to the purchaser over and above any discount, rebate, allowance, or advertising service charge available at the time of such transaction to said competitors in respect of a sale of goods of like grade, quality, and quantity; to sell, or contract to sell, goods in any part of the United States at prices lower than those exacted by said person elsewhere in the United States for the purpose of destroying competition, or eliminating a competitor in such part of the United States; or, to sell, or contract to sell, goods at unreasonably low prices for the purpose of destroying competition or eliminating a competitor.
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