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INTRODUCTION

Antitrust policy towards conglomerates assumes a new dimension when one considers the application of antitrust laws to the regulated sector.[1] Traditional antitrust criteria have been the tests of "substantial anticompetitive impacts" in these "regulatory agency-antitrust" conflicts. But the anticompetitive impacts must be weighed against other, perhaps more important, considerations in determining the net "public interest."[2] A similar procedure is suggested for evaluating true conglomerate situations. This public interest objective is unique to the regulated sector, but its extension to conglomerate situations requires less radical legislation than other proposals designed to restrict conglomerate activity.

Given the multitude of actual market contexts within which conglomeration might occur, there can be no simple, unambiguous impact of the conglomerate movement. All that can be accomplished, then, with any degree of intellectual honesty, is to ascertain central tendencies or general relationships, and to structure antitrust policy accordingly. However, general aggregative studies cannot delineate the impact of a given conglomerate relationship. More detailed analysis is required and, even then, a number of relationships will defy reliable analysis.[3]

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1 The application of antitrust to regulated companies has many of the characteristics of a conflict and precious few that would suggest the smooth orderly evolution of public policy. Several aspects, including the public interest objective, were considered in Einhorn, *Regulatory Agency — Antitrust Relationships*, 83 PUB. UTIL. FORT. 21 (1969).

2 Regulation most frequently has developed in response to conditions that seemingly required a monopolistic market structure. Regulatory agencies generally are expected to replace monopolistic market behavior with an approximation of competitive pricing — that which provides a maximum of output consistent with "normal" returns. Thus, regulatory commissions seek the general competitive objectives as well as some additional performance goals peculiar to each industry. The regulatory commissions function under statutory language unique to the regulated sector: that of recognizing the "public interest" as the primary objective of the regulatory-antitrust interaction.

3 This is clearly suggested in the regulated sector where conglomeration might adversely affect the safety of the essential regulated service, *e.g.*, by permitting the intermingling of funds from the regulated activity with the more risk-oriented capital of the unregulated sector. In addition to affecting the efficient provision of consumer service, such action could create higher barriers to entry and seriously influence effective market power.

The increasing concern (and continuing uncertainty) over the conglomerate movement's ultimate impact has led to serious proposals concerning the restriction of conglomerates, including the application of antitrust laws or per se standards of illegality.[4] Time and controversy inevitably have obfuscated both the merits and limitations of these policy alternatives. Consequently, a brief review of these alternatives can provide a context for considering a procedure comparable to that followed in the regulatory sector.

ANTITRUST ENFORCEMENT AND PER SE PROHIBITIONS AS CONSTRAINTS TO CONGLOMERATE EFFORTS

The applicability of antitrust to conglomerate companies must be considered for two separate, but interrelated circumstances: (1) internal development via company diversification, and (2) external growth via the acquisition of other companies. Each method encompasses three classes of conglomerate activity: product extension, market extension, and pure conglomerate activity. While the basic conglomerate character and corporate functions may be identical, the relevance of antitrust enforcement depends largely on whether the growth is internal or external. The clearest instances of antitrust applicability are suggested by the external acquisitions characterized as product extension and market extension mergers. These seem clearly to be covered by section 7 of the Clayton Act[5] as it relates to the restraint of potential competition. This interpretative coverage of potential competition probably is as desirable as it is (inevitably) controversial. Potentially anticompetitive conditions should be constrained even at the risk of precluding some beneficial developments. The net social cost of dissolving anticompetitive situations after the fact probably is much greater than the cost of a preventive program that inadvertently precludes situations without anticompetitive impacts or with some net benefits.[6]

There is considerable doubt as to whether internal diversification of the product extension or market extension classes (short of monopolization under section 2 of the Sherman Act[7]) is covered by the antitrust statutes. Internal efforts are not covered by section 7 of the Clayton Act, which involves only acquisitions. Nor does section 5 of the Federal Trade Act[8] seem relevant; its proscriptions of unfair practices have been permitted to

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[4] *See, e.g.*, 1968 PRESIDENTIAL TASK FORCE REPORT ON ANTITRUST, 115 CONG. REC. 5642 (daily ed. May 27, 1969); Campbell & Shepherd, *Leading-Firm Conglomerate Mergers*, 13 ANTITRUST BULL. 1361 (1968).

[5] 15 U.S.C. § 18 (1964).

[6] This view reflects (1) the rather inordinate amount of time required for settlement of antitrust issues, and (2) the difficulty of framing long delayed remedies in a meaningful manner.

For a rather comprehensive consideration of antitrust remedies, see Elzinga, *The Antimerger Law: Pyrrhic Victories?*, 12 J. LAW & ECON. 43 (1969).

[7] 15 U.S.C. § 2 (1964).

[8] 15 U.S.C. § 45 (1964).

atrophy, and in any event, its application in this situation would involve an unprecedented substitution of an enforcement agent's judgment for management discretion. Similarly, the Sherman Act is not particularly suited to conglomerate efforts since it is directed toward monopolization, and the tests of monopolization are far more rigorous than those of trade restraint. In any event, the applicability of the Sherman Act would stand on its own merits and not be related to conglomerate considerations. Pure conglomerate diversification via internal techniques is even more unlikely to involve antitrust considerations; for all practical purposes, and barring any incriminating evidence suggesting unlawful intent, internal efforts are simply not promising targets of antitrust enforcement.

In contrast, acquisitions offer a potentially fruitful area for antitrust enforcement. Enlightened enforcement, however, requires adoption of improved models of markets that would further illuminate the importance of potential competition. It may be appropriate to forestall elimination of potential competition, but such competition is relevant only when actual competition is deficient. The existence of meaningful competition diminishes the competitive importance of the incremental firm involved in a conglomerate acquisition. The difficulty of evaluating competitive conditions in antitrust situations has been described elsewhere, but it is compounded in the more ambiguous context of conglomerate markets.[9]

As yet, we have not developed an adequate analytical model in conglomerate market situations, by which one can examine such functional interrelationships as product line, relevant markets, and expected or alternative lines of business behavior. The absence of an adequate behavioral model for use in such instances only compounds the absence of meaningful objective measures for describing and ranking the extent of competition in antitrust situations. An almost necessary concomitant is an inability to determine the marginal impacts of basic structural changes upon market behavior and performance. This is the principal constraint to evaluating the significance of the structural and behavioral alternatives in controversial industry situations.

Many conglomerate cases are not amenable to an analysis of "anticompetitive" situations; the most controversial cases frequently involve companies related only in a very peripheral fashion. Thus, the public's attention may center upon apparent financial manipulation or behavior lying within the letter, but not the implicit morality or spirit, of the law. Ideally, some of these problems can be countered by measures specifically tailored to meet them; improved disclosure rules are to be preferred to antitrust enforcement as a means of allaying the concern that the formation of conglomerates reduces the amount of information available to the public, deludes investors, and so forth.

An evaluation of opportunity costs should underlie the selection of all

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[9] *See, e.g.*, H. EINHORN & W. SMITH, ECONOMIC ASPECTS OF ANTITRUST (1968).

appropriate public policies, but these costs cannot yet be meaningfully specified for conglomerate situations. Clearly, such measures must reflect the impact of each policy on growth, income distribution, and other critical aspects of our economic goals. The absence of a useful model becomes even more important in this context. Conglomerate acquisitions undoubtedly encompass a full range of competitive impacts. This should spur greater efforts to delineate the alleged benefits announced for each new conglomerate situation. Such benefits may be very real probabilities (even in a statistical sense), but they have been quite poorly presented to the courts in antitrust situations.[10]

Generally, it would be difficult, if not impossible, to formulate and implement legislation that would prohibit only those conglomerates having negative impacts. Consequently, many have suggested broad per se prohibitions of those conglomerates exceeding predetermined parameters. The particular constraints have varied, but the principle and objectives are the same for each proposal.[11]

The attractiveness of per se prohibitions is enhanced by (1) the scarcity of antitrust investigative and enforcement staff, and (2) the popular presumption that adverse economic performance is associated with conglomerate structure.[12] Unfortunately, these studies are aggregative in nature, and do not permit reliable a priori evaluations of specific conglomerate efforts. The beneficial effect of broad prohibitions is provided by their economical impact upon enforcement time and effort. Per se prohibitions probably encompass the same number of clearly anticompetitive situations as would an effective case-by-case evaluation program. One suspects that any marginally anticompetitive conglomerate acquisitions covered by per se rules would be at least offset by the automatic preclusion of some conglomerate efforts that could have proved beneficial. Limited per se rules represent a compromise of sorts. Although the guidelines promulgated by the Justice

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10 Despite the acumen underlying its complex interrelationships, the business sector has been very inept in defending the need for those proposals challenged on antitrust grounds. Most frequently, these defenses amount to a denial that any other arrangement could function equally well. Even a cursory examination of these allegations suggests their amorphous character. The economic benefits of intercorporate resource use stem from the actual use of those resources; the ownership structure does not affect the real value of these resources.

11 *See* Campbell & Shepherd, *supra* note 4. *See also* Address of Attorney General John N. Mitchell, Georgia Bar Ass'n, June 6, 1969, in 5 TRADE REG. REP. ¶ 50,247 (1969), suggesting that the Department of Justice probably would oppose any mergers by one of the top 200 manufacturing firms with another member of this group or with a leading company in a concentrated industry.

12 *See* S. REID, MERGERS, MANAGERS, AND THE ECONOMY (1968); CABINET COMMITTEE ON PRICE STABILITY, STAFF STUDIES, Paper No. 2 (Jan. 1969); FTC, STAFF ECONOMIC REPORT ON CORPORATE MERGERS, in 5 TRADE REG. REP. ¶ 50, 262 (Nov. 1969).

Recent hearings before the Senate Subcommittee on Antitrust and Monopoly of the Committee on the Judiciary have provided a wider dissemination of additional studies regarding this alleged adverse economic performance.

Department[13] and the Federal Trade Commission[14] officially approach this compromise, neither has been tested in the courts.

Traditional neoclassical economic models provide little assistance in evaluating either the immediate or long-run aspects of conglomerate transactions. Even in analyzing antitrust cases in nonregulated industries, the courts have recognized that accurate and fully quantified forecasting is neither required nor feasible.[15] The more tenuous interrelationship and the range of feasible conglomerate impacts can be evaluated only by considering the likelihood of many possible consequences. Ideally, this would be provided by a full Bayesian analysis; however, ideal solutions are not reasonable possibilities in analyzing real world problems. Generally, some less precise and more informal judgment is utilized in reaching the reasonable conclusions that comprise antitrust enforcement.

ANTITRUST STANDARDS AND REGULATED INDUSTRIES

The regulatory sector's experience with antitrust provides a number of precedents and lessons for the application of antitrust to conglomerates.[16]

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13 The Justice Department guidelines, issued at the close of the Johnson Administration, have remained dormant during the current administration. *See* Department of Justice press releases of January 26, 1968 and May 30, 1968 for statements on the merger guidelines based on market shares and the nonbinding premerger opinions. The current administration has suggested an absolute prohibition against mergers by the largest companies. *See* note 11 *supra.*

14 The FTC's merger guidelines for specific industries have been provided in a series of press releases. On January 31, 1967, guidelines were released for the food distribution and cement industries. FTC, FOOD DISTRIBUTION INDUSTRIES GUIDELINES, in 1 TRADE REG. REP. ¶ 4520 (Jan. 17, 1967); FTC, CEMENT INDUSTRY GUIDELINES, in 1 TRADE REG. REP. ¶ 4510 (Jan. 17, 1967). Subsequent guidelines have been issued for grocery products, manufacturing, and textile mill products. FTC, GROCERY PRODUCTS MANUFACTURING GUIDELINES, in 1 TRADE REG. REP. ¶ 4530 (May 15, 1968); FTC, TEXTILE MILL PRODUCTS INDUSTRY GUIDELINES, in 1 TRADE REG. REP. ¶ 4540 (Nov. 27, 1968).

15 *See, e.g.*, United States v. Penn-Olin Chem. Co., 378 U.S. 158, 175-76 (1963), wherein the Supreme Court stated:

> Unless we are going to require subjective evidence, this array of probability certainly reaches the prima facie stage. As we have indicated, to require more would be to read the statutory requirement of reasonable probability into a requirement of certainty. This we will not do.
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> . . . .
>
> Since the trial court might have been concerned over whether there was evidence on this point, we reiterate that it is impossible to demonstrate the *precise* competitive effects of the elimination of either Pennsalt or Olin as a potential competitor.

See also FTC v. Procter & Gamble Co., 386 U.S. 568, 577 (1967), wherein the Court noted:

> Section 7 of the Clayton Act was intended to arrest the anticompetitive effects of market power in their incipiency. The core question is whether a merger may substantially lessen competition, and necessarily requires a prediction of the merger's impact on competition, present and future. See Brown Shoe Co. v. United States, 370 U.S. 294; United States v. Philadelphia National Bank, 374 U.S. 321. The section can deal only with probabilities, not with certainties. Brown Shoe Co. v. United States, *supra,* at 323; United States v. Penn-Olin Chemical Co., 378 U.S. 158. And there is certainly no requirement that the anticompetitive power manifest itself in anticompetitive action before § 7 can be called into play. If the enforcement of § 7 turned on the existence of actual anticompetitive practices, the congressional policy of thwarting such practices in their incipiency would be frustrated.

16 These precedents also include situations in which commissions have the power to

The application of antitrust laws to regulated industries often has been subordinated to the regulatory authorities' responsibility to regulate in the public interest. This marriage of antitrust and regulation has been forged both by legislation and by a series of judicial rulings that competitive conditions comprise a substantial (but not the only) aspect of "the public interest." In a nonregulated industry situation, substantial anticompetitive impacts constitute violations of antitrust laws which are "against," or violative of, "the public interest." On the other hand, in regulated industries which are not exempt from antitrust enforcement, violations of the law are not synonymous with a determination of "the public interest"; the regulatory authorities can regard any factor as sufficiently important to override substantial anticompetitive impacts.[17] However, the judiciary has

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grant exemptions from the antitrust laws. *See, e.g.*, Federal Maritime Commission v. Aktiebolaget Svenska Amerika Linien, 390 U.S. 238, 245-46 (1968) wherein the Court stated:

> Congress has, it is true, decided to confer antitrust immunity unless the agreement is found to violate certain statutory standards, but as already indicated, antitrust concepts are intimately involved in the standards Congress chose. The [Federal Maritime] Commission's approach does not make the promise of antitrust immunity meaningless because a restraint that would violate the antitrust laws will still be approved whenever a sufficient justification for it exists. Nor does the Commission's test, by requiring the conference to come forward with a justification for the restraint, improperly shift the burden of proof. The Commission must of course adduce substantial evidence to support a finding under one of the four standards of § 15, but once an antitrust violation is established, this alone will normally constitute substantial evidence that the agreement is "contrary to the public interest," unless other evidence in the record fairly detracts from the weight of this factor.

17 The Supreme Court has required the full application of antitrust principles to determine whether the antitrust laws have been violated by the existence of one or more anticompetitive impacts. Such antitrust violations constitute a substantial part of the "public interest" criteria that should be served by regulatory agency opinions and ruling. It should be noted, however, that other considerations might override these antitrust violations and support the approval of the otherwise undesirable arrangement. The nature and existence of these overriding considerations must, however, be stated and justified by those seeking the benefit of this exception to the general principle. *See* United States v. First City Nat'l Bank, 386 U.S. 361 (1967), wherein the Court stated:

> First is the question whether the burden of proof is on the defendant banks to establish that an anticompetitive merger is within the exception of 12 U.S.C. § 1828(c)(5)(B) or whether it is on the Government. We think it plain that the banks carry the burden. That is the general rule where one claims the benefits of an exception to the prohibition of a statute. *Federal Trade Commission v. Morton Salt Co.*, 334 U.S. 37, 44-45. The House Report (No. 1221, 89th Cong., 2d Sess.) makes clear that antitrust standards were the norm and anticompetitive bank mergers, the exception: ". . . the bill acknowledges that the general principle of the antitrust laws — that substantially anticompetitive mergers are prohibited — applies to banks, but permits an *exception* in cases where it is clearly shown that a given merger is so beneficial to the convenience and needs of the community to be served . . . that it would be in the public interest to permit it." (Emphasis added.) *Id.* at 3-4.

Id. at 366.

> The courts are not left at large as planning agencies. The effect on competition is the standard; and it is a familiar one. If the anticompetitive effect is adverse, then it is to be excused only if "the convenience and needs of the community to be served" *clearly* outweigh it. We see no problems in bringing these standards

been increasingly strict in its acceptance of the particular consideration offered as "overriding."[18] Benefits will not be considered as overriding if they can be obtained through alternative procedures or agreements that do not infringe upon antitrust law. Only then can these benefits be evaluated to determine whether they are sufficient to overcome the substantial anticompetitive impacts.

This procedure provides a vehicle for evaluating the contrasting conglomerate forces in a flexible manner. Conglomerate relationships are more tenuous than horizontal or vertical merger situations, but these relationships can be evaluated effectively by focusing on their "net" economic impacts. While this permits companies to rebut an anticompetitive finding, it places a far greater burden upon the companies to identify benefits and to prove the necessary superiority of their programs. The difficulties will be at least comparable to those currently encountered in the regulated sector.

The elements critical to an examination of potential competition are discussed in the context of potential competition cases in the unregulated sector, and in some recent antitrust decisions involving regulated industries. The standards of the former and the evaluations of the latter are the substance of antitrust analysis required in the conglomerate sector. The former cases provide the broad standards applied by the judiciary, while the latter pivot on the weighing of competitive and other considerations to determine the public interest. Admittedly, there is no "public interest" mandate in the antimerger law, even where conglomerates are concerned; but the evaluation of conglomerate situations requires just this type of net judgment. Under these circumstances, the evaluation of competitive impact is not susceptible to the yardstick or proxy measures used in vertical or horizontal mergers. Of course, subsequent development of monopoly market power would be susceptible to attack under the Sherman Act.

One issue remains particularly unresolved and controversial in considering conglomerate efforts or acquisitions: the disposition of mergers with a neutral potential impact, *i.e.*, those having neither anticompetitive nor pro-competitive effects. This problem remains a source of conflict within the regulated sector. Regulatory agency interests frequently approve pro-

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> into the area of judicial competence. There are no constitutional problems here not present in the "rule of reason" cases.

Id. at 369-70.

Judge Wright's opinion in Northern Natural Gas Co. v. Federal Power Comm'n, 399 F.2d 953, 959-61 (D.C. Cir. 1968), contains a very compact but quite thoroughly documented examination of the relevance of antitrust law to regulatory agencies.

18 United States v. Third Nat'l Bank in Nashville, 390 U.S. 171, 189 (1967), wherein the Court noted:

> But this analysis puts aside possible ways of satisfying the requirement of convenience and need without resort to merger. If the injury to the public interest flowing from the loss of competition could be avoided and the convenience and needs of the community benefited in ways short of merger but within the competence of reasonably able businessmen, the situation is radically different. In such circumstances, we seriously doubt that Congress intended a merger to be authorized by either the banking agencies or the courts.

posals that offer no unique beneficial impacts if they are similarly free of negative impacts. In contrast, advocates of active antitrust enforcement generally will take the opposite position under such circumstances.

Depending upon who bears the burden of proof, decisions to approve (or condone) mergers will vary even if the same checklist of relevant factors is considered in each situation. If the burden of proof rests on the merging firms to show the benefits of a merger, the outcome will differ from similar circumstances in which the merger's opponents carry the burden of proving negative impacts of the merger. Thus, a "neutral" impact merger would be approved less readily if the parties were required to substantiate net or unique benefits. This procedural point is emphasized because the evidentiary burden is a particularly important determinant in the gamesmanship of both judicial and quasi-judicial regulatory proceedings. Since the economic philosophy is unambiguously pro-competitive, with monopoly power tolerated only under stringent conditions, it is not unreasonable to require proof of unique benefits as a first step in evaluating the merger of separate regulated monopolists or in evaluating conglomerate situations.

Antitrust deters the deliberate erosion of competitive market forces and provides a direct challenge to anticompetitive market situations, but antitrust per se does not directly stimulate the market process. The competitive market process receives its stimulus from lowered barriers to entry in noncompetitive markets. Many significant entry barriers have developed as a concomitant of the institutionalization of government policies; for example, tariffs restrict competition from foreign producers while, closer to home, regulatory constraints shield monopolists from technological competition. Many of these public policy objectives can be secured without restricting competitive sales efforts. Elimination of these market obstructions would stimulate competition without reducing regulatory effectiveness.

The regulatory sector's recent experiences with antitrust indicate that agency staff must apply its technical competence in this direction, *e.g.*, merger applications must be evaluated in the context of technological alternatives; thus, benefit and cost trade offs must be identified and evaluated for each alternative.[19] The significance of antitrust as a statement of basic public policy must be recognized by the regulatory authorities. This principle has received consistently increasing emphasis in recent judicial opinions, suggesting that mere lip-service to competition will not be tolerated by the

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[19] Northern Natural Gas Co. v. Federal Power Comm'n, 399 F.2d 953, 973 (D.C. Cir. 1968), wherein the Court stated:

> Moreover, the duty imposed upon the Commission by Section 7 of the Natural Gas Act is not merely to determine which of the submitted applications is most in the public interest, but also to give proper consideration to logical alternatives which might serve the public interest *better* than any of the projects outlined in the applications. *Udall v. F.P.C.*, 387 U.S. 428 (1967); *City of Pittsburgh v. F.P.C.*, *supra*, 99 U.S. App. D.C. at 123, n. 28, 237 F.2d at 751 n.28; *Scenic Hudson Preservation Conference v. F.P.C.*, *supra*, 354 F.2d at 617-620. *See generally* Reich, *The Law of the Planned Society*, 75 YALE L.J. 1227, 1248-1251 (1966).

judiciary. This concern can be extended to limit all market constraints created by, but not required for, the implementation of public policies. Extension of this concern for competitively beneficial programs would provide a greater stimulus to competition than would most proposals to restrain conglomerate efforts.

CONCLUSION

Current public policy does not provide effective evaluation and control of conglomerate companies. Neither the application of traditional antitrust law nor the per se prohibition of conglomerate acquisitions provides the necessary flexibility. Of the three types of conglomerate activity, only the product and market extension are types covered by traditional antitrust laws; the pure conglomerate is not reasonably susceptible to antitrust enforcement. Moreover, antitrust embraces only conglomerates developed through external acquisition; internal diversification is not constrained by (the civil sanctions of) antitrust statutes.

Conglomerates are characterized by several market impacts of both a beneficial and harmful character. Effective market solution is provided when each conglomerate situation is evaluated on its own merits; this procedure fully recognizes the heterogeneous nature of market situations in which no single market impact will be dominant. For this reason, conglomerates should be evaluated on a "net" basis. This procedure is used to evaluate antitrust problems in regulated industries where policy decisions must serve the public interest. Additional legislation is required to evaluate conglomerates on this basis, but such statutory authorization would be less radical than that required for other proposed restraints on conglomerates.

As a general rule, anticompetitive market potential is reduced more effectively when actual competitive forces are encouraged than when simply constraining anticompetitive forces. Competitive forces are strengthened by government policies whenever those policies are implemented without creating unnecessary market barriers. Implementation of public policies in this manner would reduce potentially anticompetitive conglomerate impacts by providing a sounder and more competitive economic environment.