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Antitrust Law--Combination in Restraint of Trade--Conspiracy to Eliminate Discount Houses as Competitors in Automobile Market Held Violative of Section 1 of Sherman Act (United States v. General Motors, 384 U.S. 127 (1966))

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RECENT DECISIONS

ANTITRUST LAW — COMBINATION IN RESTRAINT OF TRADE — CONSPIRACY TO ELIMINATE DISCOUNT HOUSES AS COMPETITORS IN AUTOMOBILE MARKET HELD VIOLATIVE OF SECTION 1 OF SHERMAN ACT. — A number of Chevrolet dealers participated in agreements with "discount houses" which enabled consumers to purchase new automobiles directly from the discounter. General Motors subjected the participating dealers to individual interviews which were sufficiently intimidating to elicit their promises to abandon these agreements with the discounters. At the insistance and with the aid of General Motors, the non-participating dealer associations pursued a policing system to insure the performance of the promises. The Supreme Court, in reversing the decision of the district court, *held* that the collaborative action to eliminate the discounters as competitors, and to deprive the participating dealers of their freedom to deal with the discounters, constituted an unlawful conspiracy in restraint of trade. *United States v. General Motors,* 384 U.S. 127 (1966).

Rapid industrial growth after the Civil War, and the ensuing growth of monopolies, forced Congress to act in order to preserve a competitive economy.[1] The first antitrust legislation passed, and the statute most widely used in litigation in this area, is the Sherman Act of 1890. Section 1 of this act provides that "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."[2] Congress drafted this section in the light of the common law and in so doing borrowed its terms and concepts.[3] Its purpose was to eliminate only those restraints on competition which constituted restraints of trade; it was not designed to eliminate those restraints which were ancilliary to a lawful business agreement.[4] Moreover, the section has no application unless three conditions precedent are met. First, there must be a contract, combination or conspiracy, *i.e.*, joint, concerted action; second, the joint action must be in restraint of

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[1] United States v. South-Eastern Underwriters Ass'n, 322 U.S. 533, 559 (1944); DOWLING & GUNTHER, CONSTITUTIONAL LAW 220 (1965).

[2] 26 Stat. 209 (1890), as amended, 15 U.S.C. § 1 (1964).

[3] See Apex Hosiery Co. v. Leader, 310 U.S. 469, 498 (1939).

[4] United States v. E.I. duPont de Nemours & Co., 188 Fed. 127, 150-51 (C.C. Del. 1911); United States v. Addyston Pipe & Steel Co., 85 Fed. 271, 280-81 (6th Cir. 1898).

interstate or foreign commerce; and third, the contract, combination or conspiracy must constitute an undue restraint of competition.[5]

The definition of joint and collaborative activity has been extremely perplexing for the Supreme Court. In *Dr. Miles Medical Co. v. John D. Park & Sons Co.*,[6] decided in 1911, the Court held that defendants' efforts to maintain the resale price of its products by means of a system of *written price maintenance contracts* violated both the common law and the Sherman Act. *United States v. Colgate*,[7] however, found no Sherman Act violation despite the fact that the manufacturer: (1) distributed to its dealers lists of resale prices to be charged, stating that no deliveries would be made to dealers who failed to comply; (2) requested information concerning non-complying dealers; (3) sought and often received promises of future adherence from offending dealers; and (4) only resumed the normal sales relations with the dealers who gave the requested promises. The Court stated that a manufacturer is entirely free to exercise discretion in choosing the parties with whom he wishes to deal.[8] This case was distinguished from *Dr. Miles* in that this indictment failed to charge the defendant Colgate with selling to the dealers under agreements.[9]

In *United States v. Schrader's Son, Inc.*,[10] the Court was confronted with a situation where a manufacturer caused its wholesalers to adhere to specified resale prices by a system of resale contracts. Relying on *Colgate*, the lower court found no breach of the Sherman Act. In reversing, the Supreme Court held that the court below had misinterpreted the *Colgate* decision, and pointed out that its indictment had failed solely because it did not charge either an express or *implied* agreement to set resale prices. Thus, *Dr. Miles* had neither been modified nor overruled.

The same rationale was reiterated in *Federal Trade Comm'n v. Beech-Nut*,[11] and *United States v. Bausch & Lomb Optical Co.*[12] In *Beech-Nut* the defendant, employing an elaborate system to enforce price maintenance policies, refused to sell to wholesalers or retailers who did not observe its prices or who sold to other dealers who did not cooperate. To enforce its policy it sought to, and succeeded in, discovering uncooperative dealers by means of the reports of other dealers, investigations of the company's agents or by a process of marking and tracing the shipments of its goods. The defendant reinstated undesirable customers

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[5] VAN CISE, UNDERSTANDING THE ANTITRUST LAWS 20-23 (1963).
[6] 220 U.S. 373 (1911).
[7] 250 U.S. 300 (1919).
[8] *Id.* at 307.
[9] *Id.* at 306-07.
[10] 252 U.S. 85 (1920).
[11] 257 U.S. 441 (1922).
[12] 321 U.S. 707 (1944).

only upon satisfactory assurances that their full cooperation would be forthcoming. In reversing the circuit court, the Supreme Court rejected the contention that the price maintenance policies were legal under the *Colgate* decision, since the practices in question went far beyond a simple refusal to sell to customers who would not resell at stated prices. A combination in restraint of trade was sufficiently established by the agreements, express or implied, between Beech-Nut and its dealers, such agreements being quite effective to accomplish "suppression of freedom of competition. . . ." [13]

Bausch & Lomb further expanded the concept of an agreement. There, the evidence showed a price maintenance scheme by means of a distribution system, whereby the distributor carefully selected and licensed wholesalers who were permitted to sell only to retailers similarly licensed. The resale prices for wholesalers were published and distributed to both wholesalers and retailers, and the wholesaler's license was revoked if unauthorized sales were made. Wholesalers were required to distribute numbered certificates with each item sold so that the distributor could easily trace unauthorized sales. The Court stated that the seller may not go beyond a simple refusal to deal with those who do not comply with the seller's policies. The seller may not, even without any agreements, suppress "freedom of competition by coercion of its customers. . . ." [14] Indeed, "whether this conspiracy and combination was achieved by agreement or by acquiescence of the wholesalers . . . is immaterial." [15]

The significance of the preceding cases was clarified by *United States v. Parke, Davis & Co.*[16] Representatives of a manufacturer of pharmaceutical products visited retailers who were advertising discount prices, and informed them that unless the suggested prices were observed the defendant would no longer deal with them. Agreements were elicited from the wholesalers to stop delivering to offending retailers and sales were only resumed after the delinquent retailer stopped selling at discount prices. The Court found a conspiracy in restraint of trade, and explained that while prior to the *Beech-Nut* decision it was necessary to find an express or implied agreement, a combination inconsistent with the Sherman Act will now be found "when the manufacturer's actions . . . go beyond mere announcement of his policy and the simple refusal to deal, and

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[13] Federal Trade Comm'n v. Beech-Nut, 257 U.S. 441, 455 (1922).

[14] United States v. Bausch & Lomb Optical Co., 321 U.S. 707, 722 (1944).

[15] *Id.* at 723.

[16] 362 U.S. 29 (1960).

he employs other means which effect adherence to his resale prices. . . ." [17]

In order to determine whether a particular joint action constitutes a conspiracy in restraint of trade, the Court initially devised the "rule of reason" test.[18] The classic definition of this test is found in *Chicago Bd. of Trade v. United States.*[19] Mr. Justice Brandeis, writing for the Court, stated that:

> Every agreement concerning trade, every regulation of trade, restrains. . . . The true test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition or whether it is such as may suppress or even destroy competition.[20]

In applying the "rule of reason," the Court considers the particular business to which the restraint is applied, "its condition before and after the restraint was imposed; the nature of the restraint and its effect, actual or probable." [21]

A second standard has been devised which is the antithesis of the "rule of reason." This is the "per se" rule and according to this standard, certain practices in restraint of trade and commerce are of such a character that they cannot be justified under any market conditions, and hence there is no need to make a showing of public injury.[22] The "per se" philosophy probably originated in *United States v. Trenton Potteries Co.*[23] There, manufacturers controlling eighty per cent of the vitreous pottery industry conspired to fix and maintain uniform prices for their products. The Court disregarded the defendants' contention that the agreement was reasonable, and stated that the practice of price fixing is not justified as reasonable simply because the fixed prices are reasonable.

In *United States v. Socony-Vacuum Oil Co.*,[24] major oil producers conspired to fix the prices of crude oil and gasoline. In affirming the Sherman Act convictions, Mr. Justice Douglas wrote: "a combination formed for the purpose and with the effect of raising, depressing, fixing, pegging, or stabilizing the price of a commodity in interstate or foreign commerce is illegal 'per se.' " [25]

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[17] *Id.* at 44.
[18] Standard Oil v. United States, 221 U.S. 1 (1911).
[19] 246 U.S. 231 (1918).
[20] *Id.* at 238.
[21] *Ibid.*
[22] "Another philosophy, the *'per se'* concept . . . has eroded the rule of reason to such an extent that it threatens to undermine its very foundation." Kalinowski, *The Per Se Doctrine—An Emerging Philosophy of Anti-Trust Law,* 11 U.C.L.A.L. REV. 569, 570 (1964).
[23] 273 U.S. 392 (1927). See *supra* note 22, at 572.
[24] 310 U.S. 150 (1940).
[25] *Id.* at 223.

The "per se" rule also has been consistently applied when a group boycott is designed solely to eliminate competition.[26] In *Fashion Originators' Guild of America, Inc. v. Federal Trade Comm'n*,[27] members of the fashion guild refused to sell to manufacturers and retailers who pirated the designs of the guild members. To effectuate this boycott, the guild members used blacklists, employed "shoppers" to visit stores to examine stocks, audited books and imposed fines. The Court rejected the defense that the practices were reasonable and stated that under these circumstances it was not necessary to hear evidence in this regard "for the reasonableness of the methods pursued by the combination to accomplish its unlawful object is no more material than would be the reasonableness of the prices fixed by unlawful combination."[28] The application of the "per se" rule to boycotts was crystallized in *Klor's Inc. v. Broadway-Hale Stores, Inc.*,[29] where a group of powerful businessmen conspired to deprive a single merchant of the merchandise necessary to compete effectively. The Court removed any doubt concerning the previously required element of intent to eliminate competition, and stated that boycotts are not saved by allegations that they are reasonable under the circumstances.

The instant case, in deciding whether the conduct of the defendants constituted a conspiracy, indicated that the question was not one of fact but rather one "of the legal standard required to be applied to the undisputed facts. . . ."[30] This legal standard is that established by *Beech-Nut, Bausch & Lomb* and *Parke, Davis & Co.*,[31] *i.e.*, the defendants in order to avoid a violation of the Sherman Act, must act unilaterally, and may not go beyond an announcement of policy and a simple refusal to sell to participating dealers.

Here, dealers' associations, acting through some of their members, complained to General Motors of the sales through discounters. Subsequently, the dealers, at an association meeting, agreed to initiate a letter-writing campaign for the purpose of bringing General Motors into the dispute. The campaign had immediate results. General Motors' personnel interviewed every Chevrolet dealer in the area and elicited a promise from each dealer that he would not do business with the discounters. Having obtained the desired promises, the dealers' associations organized the policing of the agreements. Information obtained

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[26] Note, 47 CALIF. L. REV. 383, 389 (1959).
[27] 312 U.S. 457 (1941).
[28] *Id.* at 468.
[29] 359 U.S. 207 (1959).
[30] 384 U.S. 127, 141 n.16 (1966).
[31] *Id.* at 142.

by the investigating committee was relayed to the manufacturer upon its request and used to elicit compliance from non-conforming dealers. As a result of this joint activity and the pressure which was brought to bear, a number of dealers repurchased, at a substantial loss, cars which they had previously sold through a discounter.

When measured by the correct rule, the collaborative efforts of the defendants "can by no stretch of the imagination be described as 'unilateral' or merely 'parallel.'" [32] Neither the individual dealers, the associations, nor General Motors acted independently. The dealers collaborated among themselves, through the associations and with the manufacturer, first to obtain aid from General Motors and then to enforce the promises the manufacturer induced. There was an explicit agreement to police the promises and an investigating committee worked closely with General Motors. Thus, as was the case in *Parke, Davis & Co.*, general compliance was induced by obtaining substantially interdependent promises from dealers not to do business with the discounters. These activities amounted to a "classic conspiracy in restraint of trade." [33]

The Court then pointed out what has been clear since the *Klor* decision—that a conspiracy to boycott even a single trader, is by its nature a "per se" violation of the act. The effect of the joint activities was to deprive the discounters of their free access to the automobile market. As a "per se" violation, the activity is presumed illegal without further inquiry into the economic motivation of the defendants or the possible reasonableness of the activity.

In addition, the Court found a second "per se" offense inherent in this particular combination. The record contained ample evidence that one of the conspirators' purposes was to protect the complaining dealers from price competition. Letters sent to General Motors, as part of the letter-writing campaign, contained numerous complaints about the low prices offered by the discounters. The manufacturer itself was concerned about the quotation of the discounted prices to the general public and the substantially lower interest rate charged by some of the discounters for new-car financing.

The opinion indicated that even if the trial record had not established that restraint of competition was an objective of the conspiracy, a conspiracy to remove a class of competitors from access to the market would have the equivalent effect on price competition. It too could amount to a conspiratorial restraint of price competition and hence a "per se" offense.

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[32] *Id.* at 145.
[33] *Id.* at 140.

The contracts between General Motors and its dealers contained a location clause which prohibited the franchised dealer from establishing "a different location . . . or place of business . . . without the prior written approval of Chevrolet." [34] General Motors contended that the sale to discounters was in violation of this clause and they had the contract right to prohibit it. The Court, however, because of its decision that there was a conspiracy, never reached the issue of whether the location clause prohibited the sale of autos by dealers to discounters.

Assuming *arguendo* that the location clause does prohibit the dealers from making agreements with discounters, the question arises as to whether General Motors could enforce this clause without violating the Sherman Act. Mr. Justice Harlan, concurring in the decision of the Court, believed that General Motors could legally enforce it by *unilateral* action and found nothing in the majority opinion to the contrary.[35] On the other hand, the Government argued that if the location clause is construed as including sales through the discounters it is a contract in restraint of interstate commerce and therefore its enforcement would violate the Sherman Act.[36]

The district court, interpreting the facts as meaning that General Motors was acting to enforce a contractual obligation which the dealers had assumed, reasoned that since the dealers are free to sell at any price they choose, and may compete with the other franchised dealers in the area as vigorously as they desire, the contracts did not violate the Sherman Act.[37] The court argued that to conclude otherwise would be to insist that the manufacturer's establishment of standards for its dealers consisted of an unreasonable restraint of trade. The district court found the *Chicago Bd. of Trade* rule precedent for the instant case concluding that the location clause did not suppress, but, rather, promoted competition and benefited the automobile consumer.[38]

However reasonable the argument of the district court and Mr. Justice Harlan's concurring opinion may appear as a justification for unilateral action on the part of General Motors, the hard fact still remains that the scheme does and would continue to eliminate the discounters as competitors.[39] The majority opinion in the instant case indicated that elimination of a class of traders

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[34] *Id.* at 130.
[35] *Id.* at 149.
[36] United States v. General Motors, 234 F. Supp. 85, 87-88 (S.D. Cal. 1964).
[37] *Id.* at 88.
[38] *Ibid.*
[39] The district court conceded that the plan eliminated the discounters as competitors. *Id.* at 88-89.

from access to the market was a "per se" offense. Moreover, it was indicated that any elimination by conspiracy or combination is equivalent to a conspiracy or combination to restrain price competition, a goal illegal "per se." Thus, if it is illegal to conspire to a particular end, it would seem illegal to contract to that same end.

It should be pointed out that General Motors might also encounter "conspiratorial" difficulties in attempting unilateral enforcement of the provision. In *Patterson v. United States,*[40] the court, when confronted with a conspiracy in restraint of trade on the part of the officers and agents of a corporation, held that Section 1 of the Sherman Act "includes conspiracies between competitors, or between the officers and agents of a competitor on its behalf against a competitor." [41]

If there is an unreasonable restraint on interstate commerce, it may result just as readily from a conspiracy on the part of those associated under common ownership as from a conspiracy on the part of those unassociated.[42] Thus, if the location clause, in and of itself, were found to be the product of a conspiracy within the corporate structure, it is conceivable that it would be violative of the Sherman Act.

There can be little doubt that the instant decision is in line with and controlled by *Parke, Davis & Co.* Mr. Justice Harlan concedes this in his concurring opinion, but claims that that case "represents basically unsound antitrust doctrine. . . ." [43] because that opinion for practical purposes eliminated the manufacturer's right to prescribe, in advance, the conditions upon which he will refuse to sell.[44] The instant decision, however, seems to be within the spirit of the antitrust laws and of the Sherman Act in particular, "whose purpose was . . . to make . . . so far as Congress could under our dual system, a competitive business economy." [45]

ANTITRUST LAW — MERGERS — SECTION 7 OF THE CLAYTON ACT VIOLATED BY POTENTIAL THREAT TO COMPETITION.—In an antitrust action, the United States charged that the merger of two competing grocery companies, creating the second largest chain in

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[40] 222 Fed. 599 (6th Cir. 1915).
[41] *Id.* at 618.
[42] United States v. Yellow Cab Co., 332 U.S. 218 (1947).
[43] United States v. General Motors, 384 U.S. 127, 148 (1966).
[44] See Mr. Justice Harlan's dissent in United States v. Parke, Davis & Co., 362 U.S. 29, 48 (1960).
[45] United States v. South-Eastern Underwriters Ass'n, 322 U.S. 533, 559 (1944).