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# Application of U.S. Antitrust Law to International Investment: Joint Ventures, Mergers and Acquisitions

by Bruce H. Jackson\*

## I. Introduction

When a U.S. company decides to expand its operations through investment abroad, it must keep at least one principle in mind: when it crosses the border it does not leave U.S. antitrust law behind. This article will examine the application of U.S. antitrust laws to the typical circumstances under which U.S. business invests abroad, first, through internal expansion, by establishing a division or a wholly-owned subsidiary; second, through acquisition of some or all of the stock or assets of an established foreign concern; and finally, through a joint venture with another foreign or U.S. concern. While expansion into foreign territory initially may be perceived as falling outside the reach of U.S. law, the antitrust laws in particular have been and will be applied extraterritorially when the challenged activities, despite their foreign character and geographic setting, have the requisite adverse "effect on U.S. commerce."

The primary U.S. antitrust law under which acquisitions are scrutinized is section 7 of the Clayton Act.<sup>1</sup> Section 7 prohibits any merger "in any line of commerce in any section of the country" that would "substantially . . . lessen competition, or . . . tend to create a monopoly."<sup>2</sup> Joint

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<sup>1</sup> Clayton Act, ch. 323, § 7, 38 Stat. 731 (1914) (current version at 15 U.S.C. § 18 (1976)). While sections 1 and 2 of the Sherman Act, 15 U.S.C. §§ 1-2 (1976), may also be applied on grounds that the merger constitutes a combination and conspiracy in restraint of trade and monopolization, since its amendment in 1950 to extend coverage to mergers accomplished through acquisition of assets as well as stock, section 7 has been used almost exclusively. Clayton Act, as amended by the Celler-Kefauver Act, ch. 1184, 64 Stat. 1125 (1950) (current version at 15 U.S.C. §§ 18, 21 (1976)).

Similarly, while section 5 of the Federal Trade Commission Act, ch. 33, § 5, 38 Stat. 719 (1914) (current version at 15 U.S.C. § 45 (1976)), is utilized by the FTC to challenge mergers as "unfair methods of competition," it is normally used in conjunction with section 7 allegations. In any event, it is clear that the standards developed in section 7 cases will be applied to determine whether a merger is "unfair."

<sup>2</sup> Section 7 provides, in pertinent part:

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

ventures are more likely to be scrutinized under sections 1 and 2 of the Sherman Act.<sup>3</sup> The case law, limited though it is with respect to foreign mergers<sup>4</sup> and joint ventures, makes it clear that the same principles applied in domestic cases will be applied in the international sphere.<sup>5</sup> Furthermore, as will be discussed in more detail below, the FTC and the Justice Department have continued to challenge foreign joint ventures and mergers in the courts on the grounds that they are harmful to actual or perceived potential competition.<sup>6</sup> Expanding U.S. businesses must therefore be concerned with the effect of proposed foreign investment on both actual and potential competition in U.S. commerce. Obviously to a significant degree this involves forecasting the future, but an analysis of Justice Department and FTC enforcement positions and the case decisions in the area give a company some helpful indications of where not to tread or where to tread lightly.

As an initial matter, it is clear that there will be no U.S. antitrust concerns if a U.S. company expands directly into foreign territory by means of establishing its own branch, subsidiary or affiliate.<sup>7</sup> Such a means of investment serves only to add an actual or potential competitor to the market that was not there before. Market entrance by these means is what is referred to as a *de novo* entry; it enhances competition and would be encouraged by antitrust enforcement authorities. The remaining methods of investment generally suffer from the same antitrust concerns as do domestic attempts at market expansion. Until recently that has caused difficulty for companies contemplating mergers in concentrated industries or industries where potential competition might be affected. Recent development suggest that mergers may fare a lot better today, at least in the courts.<sup>8</sup>

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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.

15 U.S.C. § 18 (1976).

<sup>3</sup> 15 U.S.C. §§ 1-2 (1976).

<sup>4</sup> The term "merger" is generally applied in reference to combinations of corporations effected in accordance with the procedures established by the corporation laws of the state where the "merger" is carried out. The term "acquisition" is broader and covers all corporate actions transferring control of property or business through the acquisition of assets or stock control over the corporation.

<sup>5</sup> See text accompanying note 27 *infra*.

<sup>6</sup> See text accompanying notes 43-53 *infra*.

<sup>7</sup> However, there can always be possible anti-monopoly concerns under section 2 of the Sherman Act, a subject beyond the scope of this article. Furthermore, the sales and marketing activities conducted through those foreign entities remain subject to U.S. antitrust scrutiny.

<sup>8</sup> Senator Kennedy introduced legislation, S. 600, 96th Cong., 1st Sess. (1979), the Small Business Protection Act, to prohibit certain large conglomerate mergers. In effect, the bill would establish a presumption that such mergers are anticompetitive by shifting the burden of proving a lack of adverse effect to the merging companies. Both the Justice Department and the FTC have indicated support for some type of new legislation to deal with conglomerate mergers. See 905 ANTITRUST & TRADE REG. REP. (BNA) A-13, Mar. 15, 1979.

## II. Acquisitions and Mergers

When embarking on a program of foreign acquisitions, U.S. companies should be concerned initially with potential adverse government enforcement activity. This analysis therefore begins with the Justice Department's *Antitrust Guide for International Operations*.<sup>9</sup> In Case Study B,<sup>10</sup> for example, the Justice Department considers the hypothetical acquisition by the largest U.S. and international manufacturer of razor blades of a small German manufacturer that has developed a specialty steel blade. While the Justice Department notes that section 7 of the Clayton Act theoretically applies to such an acquisition if it would foreclose or eliminate substantial competition in any relevant market in the United States, it states that application would be unlikely here because the German company is not "engaged in commerce," that is, engaged in production, distribution, or acquisition of goods or services in commerce among the states or between the United States and a foreign country.<sup>11</sup> Furthermore, the Justice Department points out that, if the German manufacturer were "engaged in commerce," its acquisition might violate U.S. antitrust law if it were found to be major *potential entrant* into the U.S. market. The Justice Department position is simply, and no doubt correctly, stated. Yet, it is not so easily interpreted or applied by a businessman ready to expand into foreign territory by means of acquisition. Simply stated, to violate section 7 the acquiring and acquired companies must be "engaged in commerce," and the acquisition must have a substantial adverse effect on either actual or potential competition in the relevant market. It is important to examine these criteria closely.

### A. Engaged in Commerce

The initial question under section 7 with respect to foreign expansion is a jurisdictional one. Since both the acquiring and acquired companies must be "engaged in commerce,"<sup>12</sup> in the circumstances of a foreign acquisition by a U.S. company, for example, the statutory lan-

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<sup>9</sup> ANTITRUST DIVISION, U.S. DEP'T OF JUSTICE, *ANTITRUST GUIDE FOR INTERNATIONAL OPERATIONS* (rev. ed. 1977) [hereinafter cited as *ANTITRUST GUIDE*].

<sup>10</sup> The complete facts of Case B are as follows:

Razors, Inc. ("RI"), an American company, is the largest manufacturer of razor blades both in the United States and internationally, accounting for about half of all U.S. and world sales. RI proposes to buy Glint, a small German specialty manufacturer, which has developed a cadmium steel razor blade arguably superior to the traditional steel blades offered by RI and the other major companies here and abroad. Glint has started selling these blades in Germany (but on a low advertising budget) and still accounts for less than 1% of all razor blade sales in Germany. Its export sales to the United States are insignificant. RI independently possesses the technical capability to manufacture cadmium blades, but it has decided against doing so either in the United States or abroad.

*Id.* at 15.

<sup>11</sup> In addition the Justice Department notes that "[t]he 'engaged in commerce' limitation will prevent the application of section 7 to those international acquisitions where, as here, the foreign party is small and not directly operating in the United States." *Id.* at 16.

<sup>12</sup> *United States v. American Bldg. Maintenance Indus.*, 422 U.S. 271, 283 (1975).

guage appears to require that the foreign company already be either selling into or importing from the United States, or at least have some other direct contact with U.S. or foreign commerce. This has been true in the decisions to date,<sup>13</sup> but there have been few cases involving foreign acquisitions on which to base any black-letter conclusions.<sup>14</sup>

### *B. Relevant Market*

Since section 7 will be violated only if the activity involved may substantially lessen competition or tend to create a monopoly in a "line of commerce," all acquisitions require a threshold determination as to the relevant product and geographic market. The relevant product market will include those products that are reasonably interchangeable for the same use and with respect to which pricing characteristics exhibit a cross-elasticity of demand<sup>15</sup> between the products.<sup>16</sup> It is recognized, however, that there may exist well-defined sub-markets that will constitute separate markets for antitrust purposes.<sup>17</sup>

The Supreme Court has not had occasion to address the relevant geographic market requirement in an international merger case. In the domestic area, the key decision is *Brown Shoe Co. v. United States*<sup>18</sup> where the Court indicated the existence of a close relationship between product and geographic markets for section 7 purposes.<sup>19</sup> The Court held "the

<sup>13</sup> See, e.g., *United States v. Joseph Schlitz Brewing Co.*, 253 F. Supp. 129, 138 (N.D. Cal. 1966), *aff'd per curiam*, 385 U.S. 37 (1966), *rehearing denied*, 385 U.S. 1021 (1967) (where the court considered the continuous flow of beer from Labatt Canada to the U.S. and Labatt's close business relationship with a U.S. company as evidence of engaging in commerce); *Brunswick Corp.*, 942 ANTITRUST AND TRADE REG. REP. (BNA) F-1, F-4 (December 6, 1979) (involving application of Section 7 to a joint venture).

<sup>14</sup> At least one commentator has suggested that the courts may apply a more liberal standard if the acquisition has "an overall substantial impact on U.S. trade." W. FUGATE, *FOREIGN COMMERCE AND THE ANTITRUST LAWS* 335 (2d ed. 1973). Also, while section 5 of the FTC Act requires only an "effect on commerce," this law has not been used by itself to invalidate an acquisition.

<sup>15</sup> Cross-elasticity of demand is present when as the price of one product increases, demand for a reasonably interchangeable product also increases and vice-versa.

<sup>16</sup> *Brown Shoe Co. v. United States*, 370 U.S. 294 (1962). These concepts were originally formulated by the Supreme Court to determine whether products were competitive with one another within the meaning of section 2 of the Sherman Act. See *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377 (1956).

<sup>17</sup> *Brown Shoe* indicates that the principal factors to be considered in determining the existence of a separate sub-market are:

- (1) industry or public recognition of a submarket as a separate economic entity;
- (2) the products' peculiar characteristics and uses;
- (3) unique production facilities;
- (4) distinct customers;
- (5) distinct prices;
- (6) sensitivity to price changes;
- (7) specialized vendors.

370 U.S. at 325.

<sup>18</sup> 370 U.S. 294.

<sup>19</sup> The Court has stated that the "criteria to be used in determining the appropriate geographic market are essentially similar to those used to determine the relevant product market." *Id.* at 336.

geographic market selected must . . . both 'correspond to the commercial realities' of the industry and be economically significant. Thus, although the geographic market in some instances may encompass the entire nation, in some other circumstances, it may be as small as a single metropolitan area."<sup>20</sup>

Similarly, in *United States v. Philadelphia Nat'l Bank*<sup>21</sup> the Court defined the geographic market as the "area in which the seller operates, and to which the purchaser can practically turn for supplies."<sup>22</sup> More recently, in *United States v. Marine Bancorporation, Inc.*,<sup>23</sup> the Court held that the relevant geographic market is the section of the country where "the goods or services at issue are marketed to a significant degree by the acquired firm."<sup>24</sup> Thus it appears that the courts will continue the trend initiated in *Brown Shoe* and select national, regional and local geographic markets on the basis of economic and commercial realities, and that these criteria will be applied equally to the international acquisition.<sup>25</sup>

### C. Criteria for Determining Illegality

#### 1. Historical Development

Once the relevant product and geographic markets are determined, it is necessary to determine whether the requisite anticompetitive effects are likely to occur in these markets as a result of the acquisition. The primary focus of government enforcement action under section 7 of the Clayton Act is on promoting and preserving those "market structures" that are conducive to competition. Accordingly, in order to assess the legality of a corporate acquisition, one must analyze it in light of the market structure that will be affected. For this purpose acquisitions have been characterized as horizontal, where a company acquires a firm that is a direct competitor in the same product line in the same geographic area; vertical, where a company acquires a customer or supplier; and conglomerate, where the acquired company is neither a competitor nor has a supplier/purchaser relationship with the acquiring company.<sup>26</sup>

<sup>20</sup> *Id.* at 336-37.

<sup>21</sup> 374 U.S. 321 (1963).

<sup>22</sup> *Tampa Elec. Co. v. Nashville Coal Co.*, 365 U.S. 320, 327, *cited in* 374 U.S. at 359.

<sup>23</sup> 418 U.S. 602 (1974).

<sup>24</sup> *Id.* at 620-21.

<sup>25</sup> At least one commentator has suggested that the rationale of *Brown Shoe* and *Marine Bancorporation* is "capable of supporting a relevant geographic market which extends past the United States borders to incorporate the area of international competition." Yoerg, *Foreign Entry and the Potential Competition Doctrine Under Section 7 of the Clayton Act*, 46 ANTITRUST L.J. 973, 990 n.73 (1978), and cases cited therein.

<sup>26</sup> Conglomerate mergers may be further subdivided as follows:

(1) Product Extension—where the products of the acquired company are complementary to those of the acquiring company and may be produced with similar facilities, marketed through the same channels in the same manner and advertised by the same media;

The following are the principal factors which the courts have considered in assessing the legality of various types of acquisitions:

- (1) Degree of concentration or trends toward concentration in an industry;
  - (2) Conditions of entry; that is, the ease with which new competitors may enter the market; and
  - (3) Probable effect of the merger on potential competition.<sup>27</sup>
- It is important to understand how these criteria have been applied to the various types of acquisitions.

#### *a. Industry Concentration*

Of the various types of mergers, the easiest to analyze is the horizontal acquisition, which involves the merger of competitors. In these cases, the Supreme Court has in the past stressed market share statistics, concentration ratios and industry concentration trends. Thus, in *United States v. Philadelphia Nat'l Bank*<sup>28</sup> the Supreme Court stated:

Specifically, we think that a merger which produces a firm controlling an undue percentage share of the relevant market and results in a significant increase in the concentration of firms in that market is so inherently likely to lessen competition substantially that it must be enjoined in the absence of evidence clearly showing that the merger is not likely to have such anticompetitive effects.<sup>29</sup>

Even more rigid standards have been imposed where a trend toward concentration is evidenced in an industry. Under these circumstances a violation of section 7 has been found to exist even where the combined market shares of the acquired and acquiring firms are relatively small. For example, in *United States v. Von's Grocery Co.*<sup>30</sup> the Supreme Court invalidated an acquisition where the combined market share of the merged companies amounted to only 7.5%. The rationale was that the

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(2) Geographic Market Extension—where the acquiring and acquired companies sell the same products or are in similar businesses but in different geographic areas; and

(3) Pure Conglomerate—where there is no discernable economic relationship between the businesses of the acquiring and acquired firms.

<sup>27</sup> See, e.g., *FTC v. Proctor & Gamble Co.*, 368 U.S. 568 (1967); *United States v. El Paso Natural Gas Co.*, 376 U.S. 651 (1964); *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321 (1963).

<sup>28</sup> 374 U.S. 321 (1963).

<sup>29</sup> *Id.* at 363. See, e.g., *United States v. Phillipsburg Nat'l Bank and Trust Co.*, 399 U.S. 350 (1970) (finding that in an already concentrated market, the merger of two small banks would only increase concentration); *United States v. Continental Can Co.*, 378 U.S. 441 (1964) (finding a section violation where the acquiring company increased its market share by 3.1% to 25% by means of the acquisition); *United States v. Aluminum Co. of America*, 377 U.S. 271, *rehearing denied*, 377 U.S. 1010 (1964) (finding a section 7 violation where a firm with 27.8% of the market acquired a competitor with only 1.3% of the market); *Abex Corp. v. FTC*, 420 F.2d 928 (6th Cir. 1970), *cert. denied*, 400 U.S. 865 (1970) (invalidating the acquisition of an industry leader by the third largest firm in the market); *United States v. Amax, Inc.*, 402 F. Supp. 956 (D. Conn. 1975) (invalidating a merger between the fifth and seventh largest copper refiners).

<sup>30</sup> 384 U.S. 270 (1966).

number of single store retail groceries had steadily decreased and the number of grocery chains had dramatically increased; thus, a "trend" toward concentration was established.<sup>31</sup> Similarly, in *United States v. Pabst Brewing Co.*<sup>32</sup> the Supreme Court invalidated the merger of two leading nationwide brewers where their combined market shares after acquisition would amount to only 4.49%.

The courts also consider the existence of a trend towards concentration or vertical integration in an industry a key factor in determining the legality of a vertical acquisition.<sup>33</sup> Although a vertical integration will not result directly in the loss of a competitor from the market place, the vertical integration of one competitor with its suppliers or customers significantly reduces the access of other competitors to those suppliers or markets, which in the long run affects competition. This is particularly true in a highly concentrated market.

Until recently these decisions suggested that a virtual *per se* rule of illegality existed whenever there was a trend toward concentration in any market and two significant competitors in that market decided to merge.<sup>34</sup> In fact, the one prediction that could be made most securely with respect to horizontal merger enforcement cases was that the government view would always prevail.<sup>35</sup> Recent decisions of the Supreme Court<sup>36</sup> and certain lower courts<sup>37</sup> suggest that this is no longer the case.<sup>38</sup> This trend will be discussed in more detail below.<sup>39</sup>

<sup>31</sup> *Id.* at 277-79.

<sup>32</sup> 384 U.S. 546 (1966).

<sup>33</sup> *See, e.g.*, *Ford Motor Co. v. United States*, 405 U.S. 562 (1972); *Brown Shoe Co. v. United States*, 370 U.S. 294, 332 n.57 (1962); *United States v. Sybron Corp.*, 329 F. Supp. 919 (E.D. Pa. 1971); *United States v. Kimberly-Clark Corp.*, 264 F. Supp. 439 (N.D. Cal. 1967); *United States v. Standard Oil Co. (N.J.)*, 253 F. Supp. 196 (D.N.J. 1966).

<sup>34</sup> Helping to foster this trend is the Justice Department's merger guidelines. *See* DEPT OF JUSTICE, MERGER GUIDELINES (May 1968), reprinted in 1 TRADE REG. REP. (CCH) ¶ 4510 [hereinafter cited as MERGER GUIDELINES]. These guidelines closely follow the court decisions in applying concentration statistics. For example, where markets are highly concentrated, *i.e.*, the four largest firms have 75% or more of the market, the Department will ordinarily challenge mergers where the acquired or acquiring companies each account for as little as 4% of the total market.

<sup>35</sup> The federal government's record caused Justice Stewart to comment that the one consistent thread running through antimerger cases was that the government always won. *United States v. Von's Grocery Co.*, 384 U.S. 270, 301 (1965).

<sup>36</sup> *United States v. Marine Bancorporation*, 418 U.S. 602 (1974); *United States v. General Dynamics Corp.*, 415 U.S. 486 (1974).

<sup>37</sup> *See, e.g.*, *United States v. International Harvester Co.*, 564 F.2d 769 (7th Cir. 1977); *United States v. Consolidated Foods Corp.*, 455 F. Supp. 108 (E.D. Pa. 1978); *United States v. Culbro Corp.*, 436 F. Supp. 746 (S.D.N.Y. 1977); *United States v. Federal Co.*, 403 F. Supp. 161 (W.D. Tenn. 1975); *United States v. M.P.M., Inc.*, 397 F. Supp. 78 (D. Colo. 1975).

<sup>38</sup> Commentators have suggested that this recent trend has destroyed effective government merger enforcement. *See* Kolb, *The Impact of Business Realities in Recent Potential Competition and Horizontal Merger Cases—The Government Can Lose*, 47 ANTITRUST L.J. 955 (1978); Brodley, *Potential Competition Mergers: A Structural Synthesis*, 87 YALE L.J. 1 (1977).

<sup>39</sup> *See* notes 62 through 71 and accompanying text *infra*.

### *b. Conditions of Entry*

Another key criterion applicable to virtually all types of acquisitions is that of entry conditions; that is, the ease with which new competitors may enter a given industry, both before and after a merger. While conditions of entry have not weighed heavily in horizontal merger cases, since courts have stressed market share statistics and industry concentration trends, they have been an important factor in cases involving vertical acquisitions.<sup>40</sup> In *FTC v. Proctor & Gamble Co.*<sup>41</sup> the Supreme Court stressed the effects that the acquisition of Clorox would have on smaller firms because those firms would be much more reluctant to compete with the giant Proctor & Gamble than with the smaller Clorox firm. The Court concluded that the acquisition might substantially reduce the competitive structure of the industry in that "the substitution of the powerful acquiring firm for the smaller, but already dominant, firm may substantially reduce the competitive structure of the industry *by raising entry barriers* and by dissuading the smaller firms from aggressively competing . . . ."<sup>42</sup>

### *c. Potential Competition*

Potential competition is an important concept in assessing the legality of acquisitions under section 7. The doctrine envisages a potential entrant "waiting in the wings" of a market either as a "perceived" or "actual" potential competitor. In 1964 the Supreme Court began developing the doctrine for application in merger cases, and has since continued to apply and refine it.

In *United States v. El Paso Natural Gas Co.*,<sup>43</sup> the Supreme Court

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<sup>40</sup> MERGER GUIDELINES, *supra* note 34, at Nos. 11, 12. For cases discussing entry conditions in the context of vertical acquisitions, *see, e.g.*, *Mississippi River Corp. v. FTC*, 454 F.2d 1083 (8th Cir. 1972); *U.S. Steel Corp. v. FTC*, 426 F.2d 592 (6th Cir. 1970); *United States v. Standard Oil Co.*, 253 F. Supp. 196 (D.N.J. 1966); *United States v. Aluminum Co. of America*, 233 F. Supp. 718 (E.D. Mo. 1964), *aff'd per curiam*, 382 U.S. 12 (1965); *United States v. Kennecott Copper Corp.*, 231 F. Supp. 95 (S.D.N.Y. 1964), *aff'd per curiam*, 381 U.S. 414 (1965).

<sup>41</sup> 386 U.S. 568 (1967).

<sup>42</sup> *Id.* at 578 (emphasis supplied). In his multivolume treatise on business organizations, Julian O. Von Kalinowski lists the following factors that may indicate the ease or difficulty with which a firm may enter an industry:

- (1) the amount of capital necessary to become an effective competitor;
- (2) the availability of capital;
- (3) the availability of technological developments;
- (4) the degree to which successful distribution is attributable to development of a brand or trade name;
- (5) the number and size of customers of firms already operating in the market;
- (6) the size and flexibility of demand;
- (7) the structure and nature of the industry;
- (8) the existence of federal or state regulatory statutes.

16B J. VON KALINOWSKI, BUSINESS ORGANIZATIONS—ANTITRUST LAWS AND TRADE REGULATIONS § 19.02(3), at 19-77 (1979).

<sup>43</sup> 376 U.S. 651 (1964).

considered the acquisition by El Paso, the only actual supplier of out-of-state gas for the vast California market, of Pacific Northwest, the only other important interstate pipeline west of the Rocky Mountains. The Supreme Court held that the merger violated section 7 since it foreclosed the possible entry of Pacific Northwest into the California market as an independent competitor. The Court stated:

The effect on competition in a particular market through acquisition of another company is determined by the nature or extent of that market and by the nearness of the absorbed company to it, *that company's eagerness to enter that market*, its resourcefulness, and so on. Pacific Northwest's position as a competitive factor in California was not disproved by the fact that it had never sold gas there.<sup>44</sup>

This decision was followed closely in time by *United States v. Penn-Olin Chem. Co.*<sup>45</sup> *Penn-Olin* involved the legality of a joint venture to market concentrated sodium chlorate in the southeastern United States. In holding that the joint venture violated section 7, the Supreme Court announced what is perhaps the classic statement regarding the potential competition doctrine: "The existence of an aggressive, well equipped and well financed corporation engaged in the same or related lines of commerce *waiting anxiously to enter* an oligopolistic market would be a substantial incentive to competition which cannot be underestimated."<sup>46</sup>

In application, the doctrine of potential competition is actually two theories: the "perceived entrant" and the "actual potential entrant." In the case of the perceived entrant, competitive influence is exerted on firms in the market because they perceive a potential entrant on the edge of the market. Accordingly, these firms will in theory refrain from using their market power to obtain the highest level of profits because they want to discourage the firm on the edge of the market from entering and becoming a direct competitor. The Supreme Court has expressly accepted the perceived potential entrant theory.<sup>47</sup>

Conversely, the actual potential entrant theory<sup>48</sup> does not deal in perception. Rather, the hypothesis is that the acquisition of the potential entrant on the edge of a concentrated market eliminates the possibility that the firm would actually make a future, pro-competitive entry into that market by means of internal expansion or by the acquisition of a smaller "toehold" firm.<sup>49</sup> In *Marine Bancorporation* the Supreme Court addressed, but again chose not to determine, the applicability of the actual potential entrant theory.<sup>50</sup>

<sup>44</sup> *Id.* at 660 (emphasis added).

<sup>45</sup> 378 U.S. 158 (1964).

<sup>46</sup> *Id.* at 174 (emphasis added).

<sup>47</sup> 418 U.S. 602, 624 (1974); *United States v. Falstaff Brewing Corp.*, 410 U.S. 526 (1973).

<sup>48</sup> The Supreme Court distinguished these two theories in *Falstaff*, 410 U.S. at 537.

<sup>49</sup> Toehold acquisition is entry by acquisition of a smaller firm already present in the market. See *In re Bendix Corp.*, 77 F.T.C. 731, *vacated and remanded*, 450 F.2d 534 (6th Cir. 1971).

<sup>50</sup> 418 U.S. at 639. See generally *United States v. Phillips Petroleum Co.*, 367 F. Supp. 1226, 1232 (C.D. Cal. 1973), *aff'd*, 418 U.S. 906 (1974).

Most recently, enforcement in the acquisition area has been focused on conglomerate mergers. Since a conglomerate acquisition does not have a direct or immediate effect on market concentration, the Justice Department has stated that the purpose of its enforcement activity in this area "is to prevent changes in market structure that appear likely over the course of time to cause a substantial lessening of the competition that would otherwise exist or to create a tendency toward monopoly."<sup>51</sup>

Again, the doctrine of potential competition has played a key role in the conglomerate acquisition area. The leading case holding a conglomerate merger unlawful because of the elimination of potential competition is *FTC v. Procter & Gamble Co.*<sup>52</sup> Procter & Gamble, the nation's largest seller of soaps, detergents and cleansers had acquired Clorox, by far the dominant firm in the household liquid bleach industry. The FTC brought suit, and the Court found that the liquid bleach market was heavily concentrated and that, absent the merger, Procter, the most likely prospective entrant into the market, "would have remained on the periphery, restraining Clorox from exercising its market power."<sup>53</sup>

#### *d. Other factors*

In addition to the factors discussed above relating to virtually all types of acquisitions, the following factors have been applied, *inter alia*, by the courts:

- (1) market share and rank of participating and resulting firms;<sup>54</sup>
- (2) share of market foreclosed;<sup>55</sup>
- (3) size and strength of acquiring company relative to other firms in the industry; and<sup>56</sup>

<sup>51</sup> MERGER GUIDELINES, *supra* note 34, at No. 17.

<sup>52</sup> 386 U.S. 568 (1967).

<sup>53</sup> *Id.* at 575.

<sup>54</sup> This has been applied principally to horizontal mergers. *See, e.g.,* United States v. Philadelphia Nat'l Bank, 374 U.S. 321 (1963).

<sup>55</sup> This is probably the most important factor considered in testing the legality of vertical acquisitions. By virtue of such an acquisition the competitors of the acquiring corporation may lose a potential or actual source of supply or a potential or actual customer. Thus, the Supreme Court in *Brown Shoe* stated:

Since the diminution of the vigor of competition which may stem from a vertical arrangement results primarily from a foreclosure of a share of the market otherwise open to competitors, an important consideration in determining whether the effect of a vertical arrangement "may be substantially to lessen competition, or to tend to create a monopoly" is the size of the share of the market foreclosed.

370 U.S. at 328. For further cases applying market foreclosure criteria, *see, e.g.,* Filtrol Corp. v. Slick Corp., [1970] Trade Cases ¶ 73,035 (C.D. Cal. 1969), *aff'd per curiam*, 428 F.2d 826 (9th Cir. 1970); 426 F.2d 592.

<sup>56</sup> This criterion has been applied principally in cases of vertical acquisition. *See, e.g.,* Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc., 429 U.S. 477 (1977), *vacating* NBO Indus. Treadway Cos. v. Brunswick Corp., 523 F.2d 262 (3d Cir. 1975); Reynolds Metals Co. v. FTC, 309 F.2d 223 (D.C. Cir. 1962); United States v. Aluminum Co. of America, 233 F. Supp. 718 (E.D. Mo. 1964), *aff'd per curiam*, 382 U.S. 12 (1965). With respect to conglomerate acquisitions, *see*,

(4) the probability of reciprocal dealing.<sup>57</sup>*e. Application of Criteria to Foreign Acquisitions*

As has been noted, there are few cases where section 7 has been applied to foreign acquisitions, but it seems clear that domestic merger principles will apply. The first case challenging a foreign acquisition, and perhaps the best example of the application of section 7 principles in those circumstances, is *United States v. Joseph Schlitz Brewing Co.*<sup>58</sup> In that case Schlitz Brewing Company acquired a controlling interest in John Labatt Ltd., a large Canadian brewer. The court analyzed the acquisition as if it had been wholly domestic, finding that the acquisition eliminated actual competition from the acquired firm through its wholly-owned U.S. subsidiary, General Brewing Corporation.<sup>59</sup> The court also applied the potential competition doctrine, finding that Labatt had:

the desire, the intention and the resourcefulness to enter the United States markets and to make General Brewing a stronger competitor in those markets. . . . Entry into the American brewing markets by new American firms is highly unlikely, and large established Canadian brewers represent the most probable sources of potential substantial competition in the United States markets.<sup>60</sup>

The doctrine of potential competition is of particular interest to firms contemplating international acquisitions. The Justice Department has expressed interest in using it for attacking such mergers,<sup>61</sup> and both the FTC and the Justice Department have consistently invoked the doc-

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*e.g.*, *FTC v. Procter & Gamble Co.*, 386 U.S. 568 (1967); *General Foods Corp. v. FTC*, 386 F.2d 936 (3d Cir. 1967), *cert. denied*, 391 U.S. 919 (1968); *Ekco Products Co. v. FTC*, 347 F.2d 745 (7th Cir. 1965); *United States v. Wilson Sporting Goods Co.*, 288 F. Supp. 543 (N.D. Ill. 1968).

<sup>57</sup> This criterion is applied mainly in the case of conglomerate acquisitions. The key case in this area is *FTC v. Consolidated Foods Corp.*, 380 U.S. 592 (1965), where a large food processor, wholesaler and retailer acquired the second largest producer of dehydrated onions and garlic. Since Consolidated was a substantial purchaser from food processors who, in turn, were substantial purchasers of dehydrated onions and garlic, the court found a reasonable probability that the food processors would give their onion and garlic business to the acquired company as a matter of reciprocity.

In its MERGER GUIDELINES, the Justice Department has stated that reciprocal buying is "an economically unjustified business practice which confers a competitive advantage on the favored firm unrelated to the merits of its product." MERGER GUIDELINES, *supra* note 34, at No. 19(2).

For other cases applying these criteria *see, e.g.*, *Allis-Chalmers Mfg. Co. v. White Consol. Indus., Inc.*, 414 F.2d 506 (3d Cir. 1969), *cert. denied*, 396 U.S. 1009 (1970); *United States v. General Dynamics Corp.*, 258 F. Supp. 36 (S.D.N.Y. 1966); *United States v. Ingersoll-Rand Co.*, 218 F. Supp. 539 (W.D. Pa. 1963), *aff'd*, 320 F.2d 509 (3d Cir. 1963).

<sup>58</sup> 253 F. Supp. 129 (N.D. Cal. 1966), *aff'd per curiam*, 385 U.S. 37 (1966), *rehearing denied*, 385 U.S. 1021 (1967).

<sup>59</sup> *Id.* at 144.

<sup>60</sup> *Id.* at 147-48.

<sup>61</sup> *See* ANTITRUST GUIDE, *supra* note 9, Case B at 15-18 which incorporates the standards of *Marine Bancorporation*.

trine to challenge international mergers.<sup>62</sup>

## 2. Recent Trends

### a. Market Concentration—Horizontal Mergers

While the application of pure market concentration factors leads to a virtual *per se* rule of illegality wherever significant competitors merge in a concentrated market, lower court decisions since *United States v. General Dynamics Corp.*<sup>63</sup> indicate that the courts will now look beyond mere market statistics and structural characteristics to evidence of marketing realities. In *General Dynamics*, the Supreme Court allowed an inquiry into whether market share statistics alone provide an accurate account of the acquisition's probable effect on competition.<sup>64</sup>

Accordingly, since *General Dynamics*, Justice Stewart's comment<sup>65</sup> regarding the common thread in horizontal merger cases is no longer appropriate; the Justice Department has lost as many of these cases<sup>66</sup> as it has won.<sup>67</sup> Even in cases which the Justice Department has won,

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<sup>62</sup> See, e.g., *FTC v. Mannesman A.G.*, Civ. Act. No. 79-2601 (D.D.C. Sept. 28, 1979); *United States v. Merck & Co.*, Civ. Act. No. 79-09-62-T (S.D. Cal. Aug. 17, 1979), 4 TRADE REG. REP. ¶ 45,079; *BOC Int'l Ltd. v. FTC*, 557 F.2d 24 (2d Cir. 1977); *Nestlé Alimentana, S.A.*, 3 TRADE REG. REP. (CCH) ¶ 20,808 (Dkt. No. 9003, 1975) (complaint), ¶ 21,560 (1979) (consent order); *SKF Indus., Inc.*, 3 TRADE REG. REP. (CCH) ¶ 20,961 (Dkt. No. 9046, 1975) (complaint) ¶ 21,595 (1979) (final order, acquisitions held not illegal); *BIC Pen Corp.*, 3 TRADE REG. REP. (CCH) ¶ 21,267 (Dkt. No. 9095, 1977) (complaint), ¶ 21,273 (1977) (dismissed as moot).

In his textbook, *FOREIGN COMPETITION AND THE UNITED STATES ANTITRUST LAWS*, Wilbur Fugate emphasizes the role of potential competition in the area of foreign acquisitions:

Aside from mergers between a U.S. company and a foreign company actually in the United States, the most obvious carry-over theory from domestic cases is that of potential competition, with something added: that is, the importance of foreign competition to a concentrated or oligopolistic U.S. market. Mr. McLaren, (former U.S. Attorney General) in stating this policy and interpretation of § 7, said that 'the American economy realizes substantial benefits . . . in the way of vigorous new competition, new products, new technology . . . which foreign and multinational firms are . . . enabled to offer.' He went on to say that when an existing industry is highly concentrated, 'the main pressure to keep both costs and prices down may be the existence of actual or potential competition.' Thus, 'we must be careful that the actual or potential competition posed by foreign firms is not eliminated through mergers or acquisitions.' A primary basis for a Justice merger action, then, is a situation when a foreign firm 'instead of entering on its own, or making a foothold acquisition, joins forces with a major factor in a concentrated American industry . . . .'

W. FUGATE, *supra* note 14, at 325 (footnotes omitted).

<sup>63</sup> 415 U.S. 486 (1974).

<sup>64</sup> *Id.* at 497-98. The assertion that the government's past market share statistics are really insufficient to constitute a *prima facie* case, because the acquired company is not actually as strong a competitor as the bare statistical projections would indicate, has thus become known as the "*General Dynamics* defense." See, e.g., 402 F. Supp. 956, 970 (D. Conn. 1975).

<sup>65</sup> See note 35 *supra*.

<sup>66</sup> See note 37 *supra* and accompanying text.

<sup>67</sup> *Liggett & Myers, Inc. v. FTC*, 567 F.2d 1273 (4th Cir. 1977); *FTC v. Lancaster Colony Corp.*, 434 F. Supp. 1088 (S.D.N.Y. 1977); *United States v. Mrs. Smith's Pie Co.*, 440 F. Supp.

the courts have carefully evaluated the marketing realities, notwithstanding the fact that market statistics showed the subject acquisitions to be well within the critical percentages of the Justice Department's Merger Guidelines and prior court decisions.<sup>68</sup> Recently, for example, in *United States v. International Harvester Co.*<sup>69</sup> the court of appeals considered the acquisition by International Harvester, the twenty-second largest industrial corporation in the United States and the second largest producer of agricultural machinery, of Steiger Tractor, Inc., a producer specializing in the manufacture and sale of four-wheel-drive farm tractors. While the combined market shares in four-wheel-drive tractors totalled at least twenty-two percent, the court held the the Government's *prima facie* case was effectively overcome by evidence of Steiger's financial weakness, which made its elimination as a competitor much less significant than market share alone might indicate.<sup>70</sup>

#### *b. Potential Competition*

In *United States v. Marine Bancorporation, Inc.*<sup>71</sup> the Justice Department challenged a proposed merger between two commercial banks. The acquiring bank was a large, nationally chartered bank based in Seattle. The acquired bank was a medium-sized, state-chartered bank located in Spokane. Upholding the lower court's determination that the merger did not violate section 7, the Court set forth a three-part test for determining when the potential competition doctrine may be applied based on a perceived potential entrant. First, the target market must be substantially concentrated; second, the acquiring firm must have the characteristics, capabilities and economic incentive to render it a perceived, potential *de novo* entrant; and third, the acquiring firm's premerger presence on the fringe of the target market must have, in fact, tempered the oligopolistic behavior on the part of existing participants in that market.<sup>72</sup>

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220 (E.D. Pa. 1976); *United States v. Amax, Inc.*, 402 F. Supp. 956 (D. Conn. 1976); *United States v. Blue Bell, Inc.*, 395 F. Supp. 538 (M.D. Tenn. 1975).

<sup>68</sup> In the successful government cases the post-acquisition, combined market percentage ranged from 12% to 35% in concentrated industries.

<sup>69</sup> 564 F.2d 769.

<sup>70</sup> *See also* *United States v. Consolidated Foods Corp.*, 455 F. Supp. 108 (E.D. Pa. 1978) (upholding a merger that created the third largest producer in a market and a combined market share of approximately 10%); and *United States v. M.P.M., Inc.*, 397 F. Supp. 78 (D. Colo. 1975) (upholding a merger that resulted in a combined market share of 31%). *But see* *Hittman Nuclear & Development Corp. v. Chem-Nuclear Sys., Inc.*, Civ. Act. No. N-78-2570 (D. Md. Nov. 26, 1979) (declining to follow *International Harvester* on the grounds that it is based on a misreading of *General Dynamics*).

<sup>71</sup> 418 U.S. 602 (1974).

<sup>72</sup> *Id.* at 624-25. As the Court notes:

The potential competition doctrine has meaning only as applied to concentrated

Similarly, in considering the Justice Department's contention that the challenged merger violated section 7 because it eliminated the likelihood that, but for the merger, Seattle Bank actually would have entered the Spokane market *de novo*, the Court established two prerequisites for the application of the actual potential entrant theory. First, it must be shown that the acquiring company has available feasible means for entering the market other than through the acquired company; and second, it must be shown that those means offer a substantial likelihood of ultimately producing deconcentration of that market or some other significant procompetitive effect.<sup>73</sup>

In recent lower court cases, application of the *Marine Bancorporation* standards for potential competition mergers have included detailed assessments of market performance and conduct. In each case the Justice Department lost.<sup>74</sup> In these cases the Justice Department has had difficulty establishing that the acquiring company would make a *de novo* entry into the market, or that the acquiring or acquired companies are actually perceived by those in the market as

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markets. That is, the doctrine comes into play only where there are dominant participants in the target market engaging in interdependent or parallel behavior and with the capacity effectively to determine price and total output of goods or services. If the target market performs as a competitive market in traditional antitrust terms, the participants in the market will have no occasion to fashion their behavior to take into account the presence of a potential entrant. The present procompetitive effects that a perceived potential entrant may produce in an oligopolistic market will already have been accomplished if the target market is performing competitively. Likewise, there would be no need for concern about the prospects of long-term deconcentration of a market which is in fact genuinely competitive.

*Id.* at 630-31.

<sup>73</sup> *Id.* at 633 (dicta).

Most recently, the FTC has asserted the actual potential entrant theory in its opposition to the proposed Exxon acquisition of Reliance Electric Corporation. Exxon Corp., Dkt. No. 9130 FTC (Aug. 13, 1979). The FTC claimed that acquisition of Reliance would eliminate the most likely actual *de novo* or toe-hold entrant into the market, asserting facts allegedly satisfying the criteria of *Marine Bancorporation*. The District Court for the District of Columbia issued a temporary restraining order stopping the acquisition until the merits of the case could be heard by the FTC. FTC v. Exxon Corp., Civ. Act. No. 79-1975, Memorandum Opinion (D.D.C. July 28, 1979). See 928 ANTITRUST & TRADE REG. REP. (BNA) A-3 (Aug. 23, 1979).

On August 17, 1979 the court denied the FTC's application for a preliminary injunction but exercised its inherent equitable powers to preclude Exxon from taking operational control of Reliance's motor and drive operations pending consideration of additional issues. See 401 TRADE REG. REP. (CCH) at 3-4 (Sept. 4, 1979).

The Justice Department has asserted the theory most recently in *United States v. Cross & Trecker Corp.*, Civ. Act. No. 973-737 (E.D. Mich. Sept. 25, 1979), and in *United States v. Beneficial Corp.*, Civ. Act. No. 79-C-3550 and 79-C-3551 (N.D. Ill., filed Aug. 29, 1979). See 4 TRADE REG. REP. (CCH) ¶ 45,079, case 2717 & 2718 (1979).

<sup>74</sup> *BOC Int'l, Ltd. v. FTC*, 557 F.2d 24 (2d Cir. 1977); *FTC v. Atlantic Richfield Co.*, 549 F.2d 289 (4th Cir. 1977); *FTC v. Tenneco, Inc.*, 433 F. Supp. 105 (D.D.C. 1977); *United States v. Black & Decker Mfg. Co.*, 430 F. Supp. 729 (D. Md. 1976); *United States v. Hughes Tool Co.*, 415 F. Supp. 637 (C.D. Cal. 1976); *United States v. Falstaff Brewing Corp.*, 383 F. Supp. 1020 (D.R.I. 1974).

potential entrants. For example, in *FTC v. Atlantic Richfield Co.*<sup>75</sup> the FTC contested the merger of Atlantic Richfield and the Anaconda Company on the grounds that, but for the merger, there was a "reasonable probability" that Arco would enter the copper production market by means of original entry, joint venture, acquisition of an ore body or by toehold acquisition.<sup>76</sup> The court apparently expected "unequivocal proof"<sup>77</sup> of probable entry *de novo*, holding that such entry was not feasible even for a company possessing the economic and technological resources of Atlantic Richfield.

In *BOC Int'l, Ltd. v. FTC*,<sup>78</sup> a foreign acquisition case, the FTC had ordered British Oxygen, the world's second largest producer of industrial gases, to divest itself of Airco, Inc., the third largest U.S. industrial gas producer. The FTC based its original decision on the actual potential entrant theory, finding that there was no proof of the required "wings" effect necessary to invoke the perceived potential entrant doctrine.<sup>79</sup> In setting aside the FTC divestiture order, the Second Circuit applied the *Marine Bancorporation* prerequisites. Accordingly, the court found that the probability of a *de novo* or toehold acquisition was not satisfied by the FTC's finding of a "reasonable probability of *eventual* entry,"<sup>80</sup> despite the fact that BOC had made recent *de novo* entries into other markets and had actively considered making such an entry into the U.S. market.<sup>81</sup>

Perhaps the most recent example of the government's application of the potential competition doctrine to a foreign acquisition is *SKF Indus., Inc.*<sup>82</sup> There the FTC complaint counsel challenged, *inter alia*, foreign acquisitions by the Swedish parent of SKF on the novel theory that the acquisitions were designed to eliminate foreign firms which would have competed with the U.S. subsidiary by exporting to the United States.<sup>83</sup> While the FTC termed the staff attack "imagi-

<sup>75</sup> 549 F.2d 289 (4th Cir. 1977).

<sup>76</sup> *Id.* at 292-93.

<sup>77</sup> In *Marine Bancorporation*, the Supreme Court explained that the principal focus of the potential competition doctrine has been on *perceived* potential competition rather than *actual* potential competition because "*unequivocal proof* that an acquiring firm actually would have entered *de novo* but for a merger is rarely available," thereby implying that the standard is one of "unequivocal proof" in a case where only actual potential competition is claimed. 549 F.2d at 294 (citations omitted; emphasis added).

<sup>78</sup> 557 F.2d 24 (2d Cir. 1977).

<sup>79</sup> *Id.* at 26.

<sup>80</sup> The Court reaffirmed that section 7 deals with probable anticompetitive effects on competition and not "*ephemeral possibilities*." Therefore the FTC's reference to "*eventual entry*" made the overall FTC determination one based largely on just such "*ephemeral possibilities*." *Id.* at 28.

<sup>81</sup> *Id.* at 26.

<sup>82</sup> [1973-1976 Transfer Binder] TRADE REG. REP. (CCH) ¶ 20,961 (complaint), [1976-1979 Transfer Binder] TRADE REG. REP. (CCH) ¶ 21,595 (final order; acquisitions not illegal).

<sup>83</sup> [1976-1979 Transfer Binder] TRADE REG. REP. (CCH) ¶ 21,595.

native," it held the acquisitions legal for failure to establish that the subsidiary had substantial market power or that any of the acquired companies were actually perceived as potential entrants.<sup>84</sup>

Thus, recent decisions suggest it is much less likely that the Justice Department and the FTC will be able to challenge mergers successfully based solely on market share statistical analyses or on the potential competition theory. The apparent weakening of the potential competition theory<sup>85</sup> is especially important for those companies contemplating foreign acquisitions, since it is a doctrine chiefly relied upon by both the Justice Department and the FTC in deciding foreign acquisition cases.

### III. Joint Ventures

In the event that a U.S. firm decides not to make a *de novo* entry into a foreign market and/or determines that entry by means of acquisition is either not feasible or presents potential antitrust risks, it may consider a joint venture.<sup>86</sup> A joint venture may take the form of a contractual arrangement, but more typically involves the formation of a jointly-owned subsidiary corporation.

There are a number of legitimate reasons for entering a market by way of a joint venture. These include situations where one company has skills that the other does not possess or where the investment required to enter the market is so large that the risk cannot be undertaken by one company. Sharing the risk thus may make entry feasible.<sup>87</sup>

A joint venture may have adverse antitrust implications, however. Unlike a merger, which eliminates an actual or potential competitor in

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<sup>84</sup> *Id.*

<sup>85</sup> One commentator has stated that "[t]he post *Marine Bancorporation* cases sustain the thesis that effective merger enforcement is impossible under current potential competition doctrine. Brodley, *supra* note 38, at 25.

Even the Justice Department privately concedes that if the government cannot win a potential competition case on *BOC's* facts, it may not be able to win one at all.

<sup>86</sup> 161 J. VON KALINOWSKI, *supra* note 42, § 73.09 [1], at 73-165 (1979).

<sup>87</sup> Von Kalinowski lists the following as typical reasons for utilization of a joint venture:

- (1) Combining diverse technological capabilities of companies in different industries;
- (2) Developing new sources of supply of raw materials;
- (3) Insuring sources of supply for adequate quality;
- (4) Combining availability of raw materials with the knowledge of how to convert them into complex finished products;
- (5) Raising capital by spreading the risk of losses;
- (6) Achieving economy of scale and production in marketing;
- (7) Creating new products;
- (8) Combining the sales techniques of one company with the production know-how of another;
- (9) Acquiring technical resources which are beyond the capacity of smaller single firms;
- (10) Combining technology in order to solve a common technical problem.

*Id.* § 78.08 [2], at 73-170 (1979).

the market, the joint venture actually introduces a previously non-existent competitive force into the market. Furthermore, the joint venture may enable the participating companies to undertake risks that would not be assumed otherwise, and to undertake projects that could not economically be supported by the individual entities, again introducing a competitive force into the market that would not otherwise be present. Whenever two or more companies join to act concurrently, especially where they might otherwise have acted individually, the potential effect of such a venture on a system of free competition is a concern.<sup>88</sup> Joint ventures, like acquisitions, are therefore subject to the prohibitions of the antitrust laws, particularly sections 1 and 2 of the Sherman Act and section 7 of the Clayton Act. As with acquisitions, these laws will apply extraterritorially to joint ventures between U.S. and foreign firms.

### A. Historical Development

Once again, a good place to begin an analysis is with the *Antitrust Guide*. There, the Justice Department discusses typical joint venture situations and concludes that there are three essential inquiries in determining the legality of a joint venture:

- (1) Whether the creation of the joint venture itself unreasonably restrains competition in a given market;
- (2) Whether the joint venture has any unreasonable collateral restraints; and
- (3) Whether the joint venture is in essence a "bottleneck monopoly" which must be open to all on a reasonable and non-discriminatory basis.<sup>89</sup>

With respect to the various types of joint ventures considered in the *Antitrust Guide*, joint bidding,<sup>90</sup> joint research<sup>91</sup> and joint manufactur-

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<sup>88</sup> As the Supreme Court has succinctly stated:

[The joint venture] is the chosen competitive instrument of two or more corporations previously acting independently and usually competitively with one another. The result is a "triumvirate of associated corporations." If the parent companies are in competition or might compete absent the joint venture, it may be assumed that neither will compete with the progeny in its line of commerce. Inevitably, the operations of the joint venture will be frozen to those lines of commerce which will not bring it into competition with the parents, and the latter, by the same token will be foreclosed from the joint venture's market.

United States v. Penn-Olin Chem. Co., 378 U.S. 158, 169 (1964) (footnote omitted).

<sup>89</sup> ANTITRUST GUIDE, *supra* note 9, Case C at 20.

<sup>90</sup> The facts of Case C are as follows:

Several U.S. electrical equipment manufacturers and engineering firms have established a consortium for the purpose of submitting a bid on an extremely large hydroelectric project in a Latin American country. The consortium consists of the second, third, and sixth largest U.S. equipment manufacturers (the second largest being the smaller of the two U.S. hydroelectric generator manufacturers). The consortium also includes the United States' first, fifth, and eighth largest engineering firms.

The parties have formed the consortium because the project is too large for a smaller group to finance, and a smaller group would not have the technical capabilities necessary to carry out the project. Most of the manufacturers and engi-

ing,<sup>92</sup> the Justice Department essentially concludes that it will not challenge the creation of such joint ventures if, first, they do not eliminate any significant competition between the parties themselves; second, the cost and risks associated with the project are high enough that the parties would not undertake the activity individually; third, the venture is not unduly broad in time and scope; fourth, there are no unreasonable collateral restraints of trade; and finally, the venture does not eliminate

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neers have tight capital situations and are already reasonably busy due to domestic demand and contracts made for sales and construction work in other countries. Since the project will take almost ten years to complete, the parties also are concerned with the long-run political situation in the host country.

The parties believe that they will be competing against similar consortia supported by the Japanese and British governments. Because they are anxious that U.S. firms not "cut each others' throats," several senior U.S. Government officials have been strong supporters of the proposed consortium.

The parties have not invited any other American or foreign firms to join the group; and they do not know whether other American engineering or equipment manufacturing firms know about it.

*Id.* at 19.

<sup>91</sup> The facts of Case D are as follows:

RXI, the second largest of five producers of X-metal in the United States, has entered into preliminary discussions with British Metals Ltd., one of the largest X-metal producers in the Common Market, about a research and development joint venture for the development of a process for producing X-metal from materials other than X-ore. X is available in a variety of domestic shales, but nobody has found an economic way to recover it. Several X-metal producers, including RXI and British Metals Ltd., are trying some research at the laboratory stage, but so far none has been able to develop any workable process.

The parties will form a British company, in which each would own half of the shares and appoint half the directors. The parties agree that all their research operations in this area will be conducted through the joint company. The parties have agreed that if the joint venture's research is successful, the joint company will seek to obtain patents covering its processes. RXI would be given an exclusive license to all patent rights and use of know-how in North America, while British Metals Ltd. would be given similar rights to patents in the United Kingdom, other EEC countries, and all former British colonies and dominions except Canada.

*Id.* at 23.

<sup>92</sup> The facts of Case E are as follows:

Hot Chip, Inc. is the third largest U.S. manufacturer of certain key transistor parts. It has about 22 percent of the domestic market. It has been unsuccessful in its attempts to market its transistor parts in Japan, one of the world's most important markets for the product. In order to surmount this difficulty, it has entered into a joint venture with Japan Manufacturing (JM), one of Japan's largest industrial combines. They will form a manufacturing joint venture, JZC, using Hot Chip know-how to produce completed transistors. Hot Chip will have 49 percent of the stock and half of the Board of Directors. JM will be responsible for the day-to-day operation of JZC. JM has not been in this particular field, but does manufacture a great deal of electronic equipment. Accordingly, the joint venture company will be operating on know-how licensed by Hot Chip.

Hot Chip is very concerned because JZC will have lower manufacturing costs than it has in the United States, and JM and JZC may be sources of disruption to Hot Chip's existing marketing arrangements in Australia, New Zealand, the Philippines, Europe, and the United States. Accordingly, Hot Chip has inserted into the agreement with JM a condition that neither JZC nor JM will export the transistors to the United States or other designated markets.

*Id.* at 28.

potential competition in a concentrated market.<sup>93</sup> These guidelines are essentially a distillation of the case law regarding joint ventures.

### 1. *Joint Ventures under the Sherman Act*

As has been noted, a joint venture is a combination engaged in by two or more entities to perform acts, which at least arguably could be accomplished by the entities individually. Since the Sherman Act precludes combinations of competitors which result in restraints of trade, joint ventures have been held illegal under the Act for a variety of reasons. The majority of cases that have arisen under section 1 have involved collateral restraints on the joint venture participants that constitute *per se*<sup>94</sup> violations of the antitrust laws.

A classic example of this situation is *Citizens Publishing Co. v. United States*,<sup>95</sup> where two newspapers serving the same market sought to operate a joint venture to achieve economies of production and distribution while keeping all news and editorial operations separate.<sup>96</sup> As part of the joint venture, the companies agreed to fix prices, pool profits and control the markets in which the two newspapers would operate. The Court held that these collateral restraints constituted classic *per se* violations of the antitrust laws that were not justified by the joint venture.<sup>97</sup>

Similarly, in *United States v. Topco Associates*,<sup>98</sup> the Court considered the legality of a cooperative association of regional supermarket chains, which the Justice Department challenged under section 1 of the Sherman Act. The association was formed in order for the smaller chains to compete more effectively with larger chains. Again, in addition to the joint venture itself, the participants engaged in collateral restraints—allocation of markets and customer limitations—that have been held to constitute *per se* violations of the antitrust laws.

<sup>93</sup> *Id.* at 19-32.

<sup>94</sup> The courts have long recognized that every agreement concerning trade restrains to some degree. Accordingly, they have held that only those combinations or agreements which *unreasonably* restrain are violative of the antitrust laws. *City of Chicago Bd. of Trade v. United States*, 246 U.S. 231 (1918). However, the courts have also recognized that: "there 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 . . ." *Northern Pac. Ry. Co. v. United States*, 356 U.S. 1, 5 (1958). This class of conduct is referred to as *per se* unreasonable.

<sup>95</sup> 394 U.S. 131 (1969). In reaction to this decision Congress passed the Newspaper Preservation Act of 1970, 15 U.S.C. §§ 1801-1804 (1970), exempting certain joint newspaper publishing operations from the antitrust laws. *See Newspaper Guild v. Levi*, 539 F.2d 755, 756 (D.C. Cir. 1976), *cert. denied*, 429 U.S. 1092 (1976).

<sup>96</sup> The obvious incentive for the joint venture was the fact that one newspaper was profitable while the other was losing money. *See also United States v. Paramount Pictures, Inc.*, 334 U.S. 131 (1948); *Lee Line Steamer v. Memphis, H. & R. Packet Co.*, 277 F. 5 (6th Cir. 1922); *United States v. Imperial Chem. Indus.*, 100 F. Supp. 504 (S.D.N.Y. 1951).

<sup>97</sup> 394 U.S. at 135-36.

<sup>98</sup> 405 U.S. 596 (1972).

While the Court recognized a legitimate purpose in the formation of the joint venture in order to provide an effective means of competition with larger firms, it did not find that the legitimate purpose justified the inclusion of such collateral restraints.<sup>99</sup> Thus it seems clear that in both domestic and foreign contexts joint ventures are subject to attack when the participants go beyond the legitimate purposes of the venture to engage in collateral restraints which constitute *per se* violations of U.S. antitrust law.

Joint ventures have also been held illegal under the Sherman Act where it appeared that their very purpose was to divide territories, thereby eliminating competition between the joint venture parents and perhaps adversely affecting the competitive position of non-participants.<sup>100</sup> For example, in *United States v. Minnesota Mining & Mfg. Co.*<sup>101</sup> manufacturers constituting four-fifths of the U.S. abrasives industry formed joint manufacturing subsidiaries abroad and followed a course of not exporting in competition with these foreign manufacturing concerns. The court condemned the arrangement because competition between the participants had been eliminated and the agreements precluded U.S. non-participants from receiving business they might otherwise have obtained from the foreign market.<sup>102</sup>

Similarly, in *United States v. National Lead Co.*<sup>103</sup> a joint venture company had been formed in order to manufacture and sell titanium compounds in an exclusive market. The Court held that the formation of the joint venture company was simply part of an overall territorial allocation scheme, an illegal purpose.<sup>104</sup> Finally, while recognizing the legitimate purpose of a joint venture created to afford

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<sup>99</sup> The Court stated:

The District Court determined that by limiting the freedom of its individual members to compete with each other, Topco was doing a greater good by fostering competition between members and other large supermarket chains. But the fallacy in this is that Topco has no authority under the Sherman Act to determine the respective values of competition in various sectors of the economy. On the contrary, the Sherman Act gives to each Topco member and to each prospective member the right to ascertain for itself whether or not competition with other supermarket chains is more desirable than the sale of Topco-brand products. Without territorial restrictions, Topco members may indeed '[cut] each other's throats.'

*Id.* at 610-11.

<sup>100</sup> The essence of the offense is that two or more firms, on the verge of competition in the market opt for a joint venture, thereby dividing the market between them. *United States v. Imperial Chem. Indus. Ltd.*, 105 F. Supp. 215 (S.D.N.Y. 1952); *United States v. Minnesota Mining & Mfg. Co.*, 92 F. Supp. 947, 961 (D. Mass. 1950); *United States v. National Lead Co.*, 63 F. Supp. 513, 523 (S.D.N.Y. 1945), *modified and aff'd*, 332 U.S. 319 (1947). *See* *Timken Roller Bearing Co. v. United States*, 341 U.S. 593, 597-98 (1951).

<sup>101</sup> 92 F. Supp. 947 (D. Mass. 1950).

<sup>102</sup> *Id.*

<sup>103</sup> 332 U.S. 319 (1947).

<sup>104</sup> *Id.* at 363.

economies of scale, the courts have required that where that joint venture controls an "essential facility,"<sup>105</sup> non-participants in the venture must be given non-discriminatory access to the facility.<sup>106</sup>

## 2. *Joint Ventures under Section 7 of Clayton Act*

Perhaps because much of the joint venture activity has involved conduct that constitutes *per se* violations of the antitrust laws and is thus easily reached under the Sherman Act, there has been little joint venture activity under section 7. Nonetheless, it is clear that section 7 will apply.<sup>107</sup> The landmark case in this area is *United States v. Penn-Olin Chem. Co.*<sup>108</sup> where the Supreme Court stated "[o]verall, the same considerations apply to joint ventures as to mergers, for in each instance we are but expounding a national policy enunciated by the Congress to preserve and promote a free competitive economy."<sup>109</sup> Applying the potential competition doctrine discussed earlier, the Court held that a joint venture may foreclose the possibility that one of the participants will remain on the edge of the market "continually threatening to enter."<sup>110</sup> The Court noted that under the Clayton Act there need not be proof that the joint venture purpose was to eliminate competition or that there were collateral restrictive agreements among the participants. Rather, it set forth a number of criteria courts may look to in order to determine whether there is a *probability* that the joint venture will substantially lessen competition.<sup>111</sup> Thus, virtually the same criteria that apply in determining

<sup>105</sup> This is known as a "bottleneck monopoly."

<sup>106</sup> See *Associated Press v. United States*, 326 U.S. 1, 21 (1944); *United States v. Terminal R.R. Ass'n of St. Louis*, 224 U.S. 384, 411 (1912).

<sup>107</sup> Attack under the Clayton Act will of course require as prerequisites that the participants be corporations and that the joint venture be formed by means of the acquisition of stock or assets.

<sup>108</sup> 378 U.S. 158 (1964).

<sup>109</sup> *Id.* at 170.

<sup>110</sup> *Id.* at 173.

<sup>111</sup> The Court referred to:

the probability of a substantial lessening of competition; the number and power of the competitors in the relevant market; the background of their growth; the power of the joint venturers; the relationship of their lines of commerce; the competition existing between them and the power of each in dealing with the competitors of the other; the setting in which the joint venture was created; the reasons and necessities for its existence; the joint venture's line of commerce and the relationship thereof to that of its parents; the adaptability of its line of commerce to noncompetitive practices; the potential power of the joint venture in the relevant market; an appraisal of what the competition in the relevant market would have been if one of the joint venturers had entered it alone . . . ; the effect, in the event of this occurrence, of the other joint venturer's potential competition; and such factors as might indicate potential risk to competition in the relevant market.

*Id.* at 177.

the validity of acquisitions under section 7 will apply to joint ventures, with emphasis on the potential competition doctrine.

### B. Recent Developments

There are no new developments arising out of joint venture cases themselves. Although some may question the continued vitality of *Topco Associates, Inc.*<sup>112</sup> after the Supreme Court's decision in *Continental T.V., Inc. v. G.T.E. Sylvania, Inc.*,<sup>113</sup> it appears well-entrenched for the present.<sup>114</sup> Accordingly, territorial and other *per se* restraints associated with a joint venture will remain subject to attack under section 1 of the Sherman Act if they have the requisite effect on U.S. commerce.

Perhaps the most noteworthy development here, as in the acquisitions area, is the apparent demise of the potential competition doctrine.<sup>115</sup> This is particularly important in view of the Justice Department's reliance on that doctrine in the joint venture area.<sup>116</sup> This suggests that Government attacks on joint ventures may be less likely in the future.<sup>117</sup>

## IV. Conclusion

Given the increased focus on market realities dictated by *General Dynamics* and the weakness of the potential competition doctrine following *Marine Bancorporation*, companies should perhaps actively consider acquisitions and joint ventures they would have passed up ten years ago. Additional certainty is provided by the expanded premerger notification rules.<sup>118</sup> The federal government is now in a position to make its en-

<sup>112</sup> 405 U.S. 596 (1972).

<sup>113</sup> 433 U.S. 36 (1977). There the Court overturned the traditional application of the *per se* rule to vertical territorial restraints.

<sup>114</sup> See, e.g., *Smith v. Pro Football, Inc.*, 593 F.2d 1173, 1192-93 n.8 (D.C. Cir. 1978); *Dougherty v. Continental Oil Co.*, 579 F.2d 954, 958 (5th Cir. 1978); *Outboard Marine Corp. v. Pezetel*, 461 F. Supp. 384, 401 n.34 (D. Del. 1978).

<sup>115</sup> But see *Brunswick Corp.*, 942 ANTITRUST AND TRADE REG. REP. (BNA) F-1, F-4 (Dec. 6, 1979), where the FTC recently decided that a joint venture between Brunswick and Yamaha Motor Co., Ltd. violated section 7 on account of its adverse effect on potential competition.

<sup>116</sup> See, e.g., ANTITRUST GUIDE, *supra* note 9, at 29.

<sup>117</sup> On the contrary, the FTC has recently announced its intention to increase its scrutiny of joint ventures, particularly where:

- (1) the joint venture serves as a device for exchanging price and other market data;
- (2) the joint venture may lessen potential competition;
- (3) the combined power of the joint venture partners holds substantial control over economic resources.

916 ANTITRUST AND TRADE REG. REP. (BNA) A-24 (May 31, 1979).

<sup>118</sup> Under the premerger notification rules of the Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 18(a), which apply to acquisitions and joint ventures of a requisite size, acquiring and acquired firms must produce detailed information about the proposed acquisition or venture covering areas of actual and potential competition. It should be noted that certain foreign acquisitions are exempted.

<sup>119</sup> One commentator suggests that if the Government fails to challenge proposed acquisitions at this stage, it will face increasing hostility in the courts if it attempts to overturn them at

forcement position known at an early date.<sup>119</sup> Accordingly, section 7 should now be used prospectively to block potentially anticompetitive acquisitions in their incipency.

Nonetheless, the impact of U.S. antitrust laws on acquisitions and joint ventures must not be ignored by companies considering foreign investment by these means. As was demonstrated, once the requisite "effect on U.S. commerce" is established, the concepts developed in domestic cases will, for the most part, apply equally to foreign investment. Furthermore, the FTC and the Justice Department will not hesitate to invoke these laws in international investment cases.<sup>120</sup>

### Question and Answer Period

*Mr. Jackson:* First of all, section 337 of the Tariff Act of 1930<sup>1</sup> provides U.S. domestic industries with an excellent means of challenging any suspected unfair conduct on the part of their foreign competitors who market goods in the United States. For the reasons Mr. Payne mentioned, an action under section 337 is a very short proceeding—a one-year proceeding, at most. In fact, it's really even shorter than that: the hearing must be completed within seven months, and discovery is usually closed before that. So you really have an exceptionally short period in which you can put a great deal of pressure on foreign companies: aggressive discovery can expose any unfair acts very quickly indeed.

The other possibility, of course, is to file a suit in federal court under the antitrust laws and ask for treble damages. Since the ITC has held that it need not suspend its proceedings just because the same suit is being started in federal court, plaintiffs gain a very real advantage: accelerated discovery is still available to them through the ITC proceeding, and with that plaintiffs can find out in short order whether or not they have any kind of a case, instead of spending years dragging through the typical federal court discovery process.

Another point may interest you: the Trade Agreements Act of 1979 was recently signed into law by the President. The Act is essentially the result of multilateral trade negotiations, the Tokyo Round, and it affords U.S. exporters a way of dealing with unfair trade practices of foreign governments—Japanese restrictions and product requirements on im-

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a later date. Carrell, *Annual Survey of Antitrust Developments 1977-1978*, 36 WASH. & LEE L. REV. 1, 44 (1979).

<sup>120</sup> As the Justice Department states:

The Department's most important concern is to protect the U.S. domestic market against restraints on competition—restraints on entry, pricing and terms of sale. In carrying out this effort, no essential distinction is made between domestic and foreign firms. In general, foreign firms, including state-owned or controlled firms, will be expected to observe the prohibitions of our antitrust laws, and to benefit from enforcement of those laws in the same manner as domestically incorporated enterprises.

ANTITRUST GUIDE, *supra* note 9, at 9.

<sup>1</sup> 19 U.S.C. § 1337 (1976).

ported goods, for example. If a U.S. company feels that this sort of restriction is unfair, it can start a proceeding in the Office of the Special Trade Representative and get to the bottom of the situation. It's a much better process than what we had before, and it's something U.S. companies should consider, should they feel that a foreign government is putting them at a disadvantage in the export market.

*Question:* If two U.S. companies form a joint venture for a construction job in a foreign country, and all the acts related to the venture are completed outside the United States, are any antitrust questions raised if the joint venture prevents another U.S. company from entering a bid competitive with that of the joint venture?

*Mr. Jackson:* You need to apply the criteria set forth in the Justice Department's *Guide*. This is what the courts will look to. One of those criteria involves the question of intent or purpose: Is there a legitimate purpose behind the joint venture's activities, aside from the simple desire to undersell a competitor? In other words, is the venture designed to prevent another U.S. company from making a competitive bid or is there some other legitimate reason for its formation? If it can be shown that there is a legitimate reason for entering into the joint venture, then the mere fact that another U.S. company has underbid should not necessarily make the venture illegal.

From a jurisdictional standpoint, of course, this kind of activity would be covered; federal courts have jurisdiction over the foreign commerce of the United States, and the right of a U.S. company to export to a foreign country is part of that commerce.

Assuming that there is a legitimate purpose for the venture, however, I don't think there would be an antitrust problem here.