

UNITED STATES v. BROWN SHOE CO.— A NEW TEST FOR SECTION 7?

The Clayton Act was designed to strike down certain anticompetitive practices in their incipiency, before their continued use would lead to monopoly power.¹ Specifically, the act was aimed at price discrimination,² exclusive dealing and tie-in contracts,³ mergers,⁴ and interlocking directorates,⁵ where the effect of such practices might substantially lessen competition or tend to create a monopoly.

The most recent implementation of this policy was effected by the passage of the Celler-Kefauver Antimerger Act of 1950,⁶ which amended Section 7 of the Clayton Act. Although law reviews have poured out a wealth of articles discussing and interpreting the Antimerger Act,⁷ and the Government, as of October 1960, has brought sixty-four cases under it,⁸ only one of these has reached the Supreme Court,⁹ and it was limited by its particular facts.

The Antimerger Act,¹⁰ designed to cure the alleged deficiencies in old Section 7, provides in relevant part:

1. See Edwards, *The Price Discrimination Law* 5 (1959); *American Crystal Sugar Co. v. Cuban-American Sugar Co.*, 259 F.2d 524, 526 (2d Cir. 1958), affirming, 152 F. Supp. 387 (S.D.N.Y. 1957); *United States v. Bethlehem Steel Corp.*, 168 F. Supp. 576, 582 (S.D.N.Y. 1958); H.R. Rep. No. 1191, 81st Cong., 1st Sess. 3-4 (1949); S. Rep. No. 1775, 81st Cong., 2d Sess. 4-5 (1950).

2. Clayton Act, ch. 323, § 2, 38 Stat. 730 (1914), as amended by 49 Stat. 1526 (1936), 15 U.S.C. § 13 (1958).

3. 38 Stat. 731 (1914), 15 U.S.C. § 14 (1958).

4. Clayton Act, ch. 323, § 7, 38 Stat. 731-32 (1914).

5. 38 Stat. 732 (1914), 15 U.S.C. § 19 (1958).

6. 64 Stat. 1125 (1950), 15 U.S.C. § 18 (1958).

7. See, e.g., Celler, *The New Antimerger Statute: The Current Lookout*, 36 A.B.A.J. 897 (1951); Stewart & Turner, *Significance of Oligopoly in Acquisition and Exclusive Dealing Situations Under the Clayton Act*, 25 U. Cinc. L. Rev. 427 (1956); Stigler, *Mergers and Preventive Antitrust Policy*, 104 U. Pa. L. Rev. 176 (1955); Note, *Section 7 of the Clayton Act: A Legislative History*, 52 Colum. L. Rev. 766 (1952); Note, *Quantitative or Qualitative—The Current Dilemma of Section 7 of the Clayton Act*, 44 Geo. L.J. 478 (1956); Note, *Section Seven of the Clayton Act: Undefined Weapon Against Incipient Monopolies*, 4 Kan. L. Rev. 449 (1956).

8. Handler, *Annual Review of Antitrust Developments*, 15 Record of N.Y.C. B.A. 362, 376 (1960).

9. *Maryland & Virginia Milk Producers Ass'n v. United States*, 362 U.S. 458 (1960).

10. To avoid confusion, amended Section 7 of the Clayton Act will be referred to as the Antimerger Act in the remaining portion of this article.

No corporation engaged in commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital and no corporation subject to the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets of another corporation engaged also in commerce, where in any line of commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly.¹¹

The problem of interpreting the qualifying clause, "may be substantially to lessen competition," has given rise to a spirited controversy concerning the proper standard of illegality to be applied to mergers coming within the purview of the Antimerger Act. Professor Handler articulates the problem specifically: "Is this effect [substantial lessening of competition condemned by the Act] to be measured *quantitatively* by the amount of competition disappearing as a result of a merger, or *qualitatively* by an economic analysis to determine whether there has been any impairment of the strength, health, vigor, and effectiveness of competitive forces in the market."¹²

The doctrine of "quantitative substantiality" originated in the cases which arose under Section 3 of the Clayton Act,¹³ which outlaws exclusive dealing and tie-in contracts, and contains the identical qualifying clause of Section 7. In the *International Salt* case,¹⁴ involving a tying agreement in connection with the leasing of salt machines, the Court held that an annual sales volume of \$500,000 in the "tied" product was not "insignificant or insubstantial,"¹⁵ and found a violation of the statute without any further investigation of the actual foreclosure of competitors from the market. Two years later, "quantitative substantiality" came to full fruition in the famous *Standard Stations* case.¹⁶ Defendant had exclusive supply contracts with sixteen per cent of the retail gasoline stations, selling 6.7 per cent of the gasoline,¹⁷ in a seven-state area in the West.¹⁸ Standard's six main competitors had similar exclusive supply contracts, and together, the seven major oil companies controlled seventy-six per cent of all the outlets in the area.¹⁹ Although Standard offered evidence to show that there was no substantial lessening of competition, Mr. Justice Frankfurter, writing for the majority, held that

11. 64 Stat. 1125 (1950), 15 U.S.C. § 18 (1958).

12. Handler, *Antitrust in Perspective* 58 (1957).

13. 38 Stat. 731 (1914), 15 U.S.C. § 14 (1958).

14. *International Salt Co. v. United States*, 332 U.S. 392 (1947).

15. *Id.* at 396.

16. *Standard Oil Co. v. United States*, 337 U.S. 293 (1949).

17. *Id.* at 295.

18. *Ibid.*

19. Kessler & Stern, *Competition, Contract, and Vertical Integration*, 69 *Yale L.J.* 1, 25 (1959).

such evidence was immaterial once it had been shown that competition had been foreclosed in a substantial share of the market.²⁰ Kessler and Stern have stated the rule of the case, and the rule of "quantitative substantiality" to be: "[W]hen competitors are foreclosed from a substantial enough share of the market, it is not far-fetched to infer substantial lessening of competition."²¹

There is, of course, a substantial difference between "quantitative substantiality" as used in *International Salt* and "quantitative substantiality" as used in *Standard Stations*. In the former case, the Court was only concerned with the dollar volume and found it to be "not insubstantial." In the latter case, however, the Court considered the percentage of the market which Standard controlled through its exclusive supply contracts, and in so doing considered, at least in small part, the relevant economic factors involved. In other words, the doctrine of "quantitative substantiality" as stated in *Standard Stations* involves to some extent a qualitative investigation.²²

The *du Pont-General Motors* case²³ showed an intent by the Court to apply the same test to both Sections 3 and 7 of the Clayton Act. The case was brought under old Section 7²⁴ which had been considered inapplicable to vertical mergers by the Federal Trade Commission,²⁵ the Justice Department²⁶ and the Congress.²⁷ In the *du Pont-General Motors* case, "[T]he Supreme Court discarded forty years of uniform interpretation and ruled that the scope of the original statute was not confined to horizontal acquisitions."²⁸ The Court cited *Standard Stations* and indicated that the statutory tests applicable to Section 3 were also applicable to Section 7.

Proponents of "quantitative substantiality" urge that application of this test to a merger case is in line with Congressional intent as evidenced by the committee reports on the Act,²⁹ and more important, that it has the effect of stopping a merger which threatens the competitive health of the economy, with swiftness and dispatch, thus

20. 337 U.S. at 313-14.

21. Kessler & Stern, *supra* note 19, at 28.

22. Oppenheim, Book Review, 58 Colum. L. Rev. 1100, 1102-03 (1958).

23. *United States v. E. I. du Pont de Nemours & Co.*, 353 U.S. 586 (1957).

24. Clayton Act, ch. 323, § 7, 38 Stat. 731-32 (1914).

25. FTC Report on Corporate Mergers and Acquisitions 168 (1955).

26. *United States v. E. I. du Pont de Nemours & Co.*, 353 U.S. 586, 590 (1957).

27. H.R. Rep. No. 1191, 81st Cong., 1st Sess. 11 (1949).

28. Handler, *op. cit. supra* note 12, at 50.

29. H.R. Rep. No. 1191, 81st Cong., 1st Sess. (1949); S. Rep. No. 1775, 81st Cong., 2d Sess. (1950).

comporting with the over-all policy of stopping anti-competitive acts in their incipency.³⁰

The Federal Trade Commission and the Attorney General's Committee have specifically rejected "quantitative substantiality" as applied to Section 7³¹ and Section 3³² cases, and have adopted the doctrine of "qualitative substantiality" as the correct statutory test. This doctrine finds its best expression in *Pillsbury Mills, Inc.*,³³ the first case considered by the Federal Trade Commission under the act. Here, the Commission interpreted the act as requiring "a case-by-case examination of all relevant factors in order to determine the probable economic consequences [of the merger]."³⁴ Although this approach has been highly criticized as requiring an "economic extravaganza"³⁵ in every merger case, it appears to have more merit than the *per se* approach of the "quantitative substantialists." As Professor Handler and others have pointed out,³⁶ mergers are neither good nor evil when examined in a vacuum. Each one is presented against the background of its own particular market and should be judged on its own particular merits, within the framework of the act.

The recent case of *United States v. Brown Shoe Co.*,³⁷ is particularly interesting, because it appears that the district court applied an entirely different test than those discussed above, and in so doing

30. Celler, Corporation Mergers and Antitrust Laws, 7 Mercer L. Rev. 267 (1956). See Interim Report on Corporate and Bank Mergers, Antitrust Subcommittee of the House Judiciary Committee, 84 Cong., 1st Sess. 23 (1955). For a view that the committee reports are "obscure, ambiguous and inconclusive" and if anything show congressional intent to require application of the doctrine of "qualitative substantiality," see Handler, Quantitative Substantiality and the Celler-Kefauver Act—A Look at the Record, 7 Mercer L. Rev. 279, 287 (1956).

The cases of *Dictograph Prods., Inc. v. FTC*, 217 F.2d 821 (2d Cir. 1954), affirming 50 F.T.C. 281 (1953), and *Anchor Serum Co. v. FTC*, 217 F.2d 867 (7th Cir. 1954), affirming 50 F.T.C. 681 (1954) seem to represent modified applications of the rule of "quantitative substantiality" as defined in *Standard Stations*. See generally Kessler and Stern, *supra* note 19, at 42.

31. *Pillsbury Mills, Inc.*, 50 F.T.C. 555 (1953); *Crown Zellerbach Corp.*, Trade Reg. Rep. (1957-1958 FTC Cas.) ¶ 26923 (1957); *Brillo Mfg. Co.*, FTC Dkt. 6557, Trade Reg. Rep. ¶ 27243 (1958); Att'y Gen. Nat'l Comm. Antitrust Rep. 122-25 (1955).

32. *Maico Co.*, 50 F.T.C. 485 (1953); Att'y Gen. Nat'l Comm. Antitrust Rep. 145-49 (1955).

33. 50 F.T.C. 555 (1953).

34. *Id.* at 565.

35. Interim Report on Corporate and Bank Mergers, *supra* note 30, at 23.

36. Handler, *op. cit.* *supra* note 12, at 68-69; Att'y Gen. Nat'l Comm. Antitrust Rep. 124-25 (1955).

37. *United States v. Brown Shoe Co.*, 179 F. Supp. 721 (E.D. Mo. 1959), *prob. juris. noted*, 363 U.S. 825 (1960).

has materially strengthened the Antimerger Act in its purpose of "check[ing] anticompetitive acts in their incipiency. . . ." ³⁸

In November of 1955, the United States obtained a temporary restraining order forbidding Brown from acquiring the stock of the G. R. Kinney Co., Inc., (hereinafter referred to as Kinney) the largest "family shoe store chain in the nation."³⁹ In January of 1956, the restraining order was vacated and the acquisition allowed on the condition that Kinney be operated as a separate entity.⁴⁰ The merger, under these terms, was effected on May 1, 1960. At the trial, in August of 1958, the government prevailed in its contention that the acquisition of Kinney, which produced 0.5% and sold 1.2% of the nation's shoes, by Brown, which accounted for 5% of the total shoe production, was a violation of Section 7 of the Clayton Act.⁴¹

The court found that Brown had been a leading manufacturer of men's, women's and children's shoes since 1877.⁴² Between 1929 and 1945 Brown had experimented with ownership or control of retail outlets, but had found them unprofitable and disposed of them all by 1945.⁴³ Between 1945 and 1951 Brown distributed its shoes through independent retailers, chain stores and mail order houses.⁴⁴

In 1951, Brown began acquiring various retail and manufacturing concerns, including the Wohl Shoe Co. in 1951,⁴⁵ the Weatherby-Kayser Shoe Co. in 1953,⁴⁶ and the Regal Shoe Co. in 1954.⁴⁷ In 1956, after the acquisition of Kinney, Brown became the third largest unit in the shoe industry in terms of sales, manufacturing and total assets,⁴⁸ and by 1958 owned or controlled 1,820 retail outlets.⁴⁹

During this period of expansion by acquisition and merger, there was a marked increase in the sale of Brown's products to its subsidiaries, and a corresponding decrease in the sales of other manufacturers to these subsidiaries.⁵⁰

38. *United States v. Bethlehem Steel Corp.*, 168 F. Supp. 576, 582 (S.D.N.Y. 1958).

39. 179 F. Supp. 721, 727 (E.D. Mo. 1959).

40. *United States v. Brown Shoe Co.*, 1956 Trade Cases 68244 (E.D. Mo. 1956). The court specifically refused to apply the "quantitative substantiality" test of *Standard Stations*.

41. 179 F. Supp. 721, 741 (E.D. Mo. 1959).

42. *Id.* at 724.

43. *Ibid.*

44. *Id.* at 724-25.

45. *Id.* at 725.

46. *Id.* at 726.

47. *Id.* at 725.

48. *Id.* at 727.

49. *Id.* at 737 n.9.

50. *Id.* at 725-27.

Brown, however, has not been the only member of the shoe industry moving toward vertical integration.⁵¹ As a matter of fact, there has been a general movement in the industry which is still continuing in this same direction.⁵² The large manufacturers have been steadily increasing their ownership of retail outlets, and although the court expressly found that "no one manufacturer, no one retailer, no one manufacturer-retailer combined, has a large percentage of the market, wholesale or retail . . ." ⁵³ it also found that "a small group of firms control a sizeable segment of the market."⁵⁴

Analysis of the case reveals that although the court found that the merger would substantially lessen competition in the relevant market⁵⁵ as the court defined it,⁵⁶ the main reason for its holding that the merger was in violation of the act, was the trend in the industry toward monopoly, or to be more accurate, oligopoly. The court gave great weight to Brown's previous acquisitions, and examined the Kinney merger squarely against the background of Brown's prior actions.

It appears, that had the test of "quantitative substantiality" been applied, there would have been no violation. Judge Weber admits that the percentages involved were minute.⁵⁷ It is highly unlikely that an advocate of "quantitative substantiality" could find that the acquisition of a firm with 1.2% of the nation's shoe sales by one with 5% of the total shoe production would amount to a *per se* violation because of a substantial foreclosure of the market to competitors.

On the other hand, it is not clear that a "qualitative substantiality" test, as usually applied would have resulted in a violation in this case. As previously noted, Judge Weber rested the great weight of his holding on the trend in the industry toward monopoly as evidenced by the past acquisitions of the large firms and particularly Brown. Professor Handler, considered by most to be the leading exponent of the "qualitative substantiality" doctrine, has taken great issue with the court's approach in *Brown Shoe* on the ground that the language of the act makes it "abundantly clear that the forbidden effects must result from the challenged acquisition and not from any

51. See, e.g., Kester, *International Shoe Borrows to Expand Retail Outlets*, *St. Louis Post-Dispatch*, Nov. 10, 1960, § c, p. 7, col. 2.

52. 179 F. Supp. at 737.

53. *Id.* at 739-40.

54. *Id.* at 740.

55. *Id.* at 739.

56. The court's analysis of the relevant market ("any line of commerce in any section of the country") has been criticized by Handler, *supra* note 8, at 377-78.

57. 179 F. Supp. at 737. See also note 40 *supra*.

others.”⁵⁸ Whether Judge Weber did this because he felt that a close analysis of the impact of this particular merger would not indicate a violation, is, of course, a matter of conjecture. In any event, it does seem fair to say that there is no clear indication from the facts of the case that application of the “qualitative substantiality” test would result in a holding by the court that the acquisition was in violation of the statute.

In summary, it seems doubtful that either test, as usually applied, would have resulted in a finding of a violation in this case.

Let us assume for a moment that Judge Weber had found no violation or that the Supreme Court reverses him in the coming months. If Judge Weber has analyzed the trend in the industry correctly, then we may expect to find an increasing amount of power coming into the hands of the large integrated shoe firms, and finally, within the not too distant future judging by the present rate of growth, a full blown oligopoly in the industry.

Brown Shoe would then appear to represent the unusual situation in which a leading firm is found to be heading in the direction of great economic power and control of an industry which itself is moving inexorably toward an oligopolistic structure, and yet is not subject to the sanctions of the antitrust laws designed to stop exactly this type of conduct, because neither of the tests which have been applied under the act are applicable.

The characteristics of an oligopolistic market structure, where a small number of large firms control a large segment of the market,⁵⁹ are definitely anticompetitive. Conformity among oligopolists, whether conscious or unconscious, is a salient characteristic of the market.⁶⁰ Price competition is generally nonexistent because it is uneconomic.⁶¹ As a result, price is usually set by the dominant member of the oligopoly at a level above that at which a competitive market would set it, and then followed by the other members of the market.⁶² The oligopolist functions, therefore, like a monopolist, but usually without the hazards of the antitrust laws.⁶³

An eminent authority has pointed out in a recent article that American antitrust law has been “equivocal and ineffective” in its

58. Handler, *supra* note 8, at 380.

59. Kaysen & Turner *Antitrust Policy—An Economic and Legal Analysis* 27 (1959).

60. See Lindahl & Carter, *Corporate Concentration and Public Policy* 388-408 (3d ed. 1959); Dow, *The Supreme Court, The “New Competition,” and “Reasonable Behavior,”* 13 *Okla. L. Rev.* 174, 177 (1960).

61. Lindahl & Carter, *op. cit. supra* note 60, at 393-94.

62. *Id.* at 397-98.

63. Wilcox, *Public Policies Toward Business* 845 (1955).

response to the problem of oligopoly.⁶⁴ In its "ineffective and equivocal fashion," Antitrust has dealt with mature oligopolies by developing such devices as "exclusive dealing,"⁶⁵ "price leadership,"⁶⁶ "conscious parallelism"⁶⁷ and "intra-enterprise conspiracy."⁶⁸ As proof extant that these devices have been less than completely effective, one can turn to such oligopolistic industries as steel,⁶⁹ aluminum,⁷⁰ automobiles,⁷¹ salt⁷² and meat products,⁷³ to mention just a few. A number of suggestions have been put forward for control of full blown oligopolies, all of which, however, require substantial amendments to the presently existing law.⁷⁴

The discussion above would seem to indicate that under the present interpretation of the antitrust laws, the government has poor weapons for dealing with oligopolists and none for dealing with incipient oligopolists who advance toward their goal by a series of small acquisitions rather than by merger with other giants in their industry.

In view of the probable failure of either of the two major tests under the act, when applied to the *Brown Shoe* situation, it appears that Judge Weber's test which goes beyond the impact of the particular merger before the court, and enlarges the permissible scope of the inquiry to include the previous acquisitions of the company and the trend in the industry, is useful, reasonable and worthy of adoption. The economy can not countenance the continuous, gradual

64. Schwartz, *New Approaches to the Control of Oligopoly*, 109 U. Pa. L. Rev. 31, 41 (1960).

65. *Standard Oil Co. v. United States*, (Standard Stations) 337 U.S. 293 (1949) (defendant controlled twenty-three percent of the sales in its region and all other major suppliers followed its practices).

66. *American Tobacco Co. v. United States*, 328 U.S. 781 (1946) (largest three cigarette companies followed each other's prices).

67. *Interstate Circuit, Inc. v. United States*, 306 U.S. 208 (1939) (common terms of licensing second run showings of films of dominant movie producers).

68. *Kiefer-Stewart Co. v. Joseph E. Seagram & Sons, Inc.*, 340 U.S. 211 (1951) (parent and subsidiaries ordered not to collaborate on prices).

69. The twelve largest companies control 83% of the industry capacity. *United States v. Bethlehem Steel Corp.*, 168 F. Supp. 576, 584 (S.D.N.Y. 1958).

70. The "big three" (Alcoa, Reynolds and Kaiser) control 96% of the virgin aluminum market. Lindahl & Carter, *op. cit. supra* note 60, at 219.

71. General Motors, Ford and Chrysler produce over 95% of the automobiles sold in the United States. Shubik, *A Game Theorist Looks at the Antitrust Laws and the Automobile Industry*, 8 *Stan. L. Rev.* 594, 616 (1956).

72. The eight largest companies control 93% of the market. Kaysen & Turner, *op. cit. supra* note 59, at 280.

73. The three largest firms control 64% of the industry's net capital assets. *FTC Report on the Concentration of Productive Facilities* 17 (1947).

74. See, e.g., Schwartz, *supra* note 64, at 47; Kaysen & Turner, *op. cit. supra* note 59, at 111-41.

foreclosure of competition, merely because the available tests for interpretation of the act are inadequate; since in the long run, the effects are identical with the conduct which the act would strike down.

Perhaps a final quote from Judge Weber will best illustrate his philosophy of the case, and its importance to the effectiveness of antitrust enforcement:

We can only eat an apple a bite at a time. The end result of consumption is the same whether it be done by quarters, halves, three-quarters, or the whole, and is finally determined by our own appetites. A nibbler can soon consume the whole with a bite here and a bite there. So, whether we nibble delicately, or gobble ravenously, the end result is, or can be, the same.⁷⁵

75. *United States v. Brown Shoe Co.*, 179 F. Supp. 721, 740 (E.D. Mo. 1959).