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Carol A. Doyle

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INTRODUCTION

Conglomerate merger activity has dominated the current post-World War II merger movement. In 1950, only thirty-eight per cent of all mergers were conglomerate in nature. More recently, however, conglomerate mergers have accounted for eighty to ninety per cent of all mergers. Although merger activity declined after reaching a peak level in 1969, a significant new merger movement,

1. The term "conglomerate merger" originally referred to a merger between two companies in completely unrelated fields of business. Conglomerate mergers are now generally defined as all acquisitions which are not principally horizontal or vertical in nature. See Bauer, Challenging Conglomerate Mergers Under Section 7 of the Clayton Act: Today's Law and Tomorrow's Legislation, 58 B.U.L. Rev. 199, 200 n.7 (1978) [hereinafter cited as Bauer]. A horizontal merger is one between firms producing identical products or close substitutes for the same geographic market. See Turner, Conglomerate Mergers and Section 7 of the Clayton Act, 78 Harv. L. Rev. 1313, 1315 (1965) [hereinafter cited as Turner]. A vertical merger is one between a supplier and a purchaser of a product. Id.

Conglomerate mergers are subdivided into three categories: (1) product extension mergers between companies whose products are related but are not in direct competition; (2) geographic extension mergers between companies who produce the same product but for different geographic markets; and (3) "pure" conglomerate mergers between companies whose products are completely unrelated. See Bryan, Conglomerate Mergers: Proposed Guidelines, 11 Harv. J. Legis. 31, 32 (1973) [hereinafter cited as Bryan].

2. In contrast, mergers involved in the first two great merger movements in United States history, occurring from 1898 to 1903 and from 1925 to 1930, were principally horizontal and vertical in nature. See Note, Clayton § 7 and the Pure Conglomerate: The Business of Buying Businesses, 35 U. Pa. L. Rev. 115 (1973).


4. A distinctive feature of the current merger movement involves the type of companies participating in it. Although conglomerate merger activity in the 1960's was carried on predominantly by a limited number of aggressive, high-growth firms such as Gulf & Western Industries, Inc., International Telephone & Telegraph, Inc., and Levy-Temco-Vought, Inc., and was regarded as "faintly disreputable," the economic establishment has joined in the recent merger surge as evidenced by the Mobil Oil-Marcor, Inc., Kennebec Copper-Carbordum Corporation, and Philip Morris-Miller Brewing mergers. See Pertchuk and Davidson, What's Wrong with Conglomerate Mergers, 11 Antitrust L. & Econ. Rev. 67 (1979) [hereinafter cited as Pertchuk and Davidson]. See also Winter, Conservative Firms Bent on Profit Growth Join the Merger Cause, Wall St. J., Apr.11, 1978, at 1, col. 6.

5. A record number of 6,107 mergers and acquisitions were announced in 1969. See 973 Antitrust & Trade Reg. Rep. (BNA) AA-2 (July 17, 1980). After 1969, however, economic
beginning in 1977 and continuing to the present, has aroused considerable economic, political, and social concern. Significantly, although this current movement is of a lesser magnitude than the 1960's movement, there has been a dramatic increase in the number of large mergers involving a purchase value of over $100 million.

Aggregate concentration has increased concomitantly with conglomerate during the past twenty years. The top 200 manufacturing firms increased their share of national sales from forty-one percent in 1955 to sixty-six per cent in 1977. Federal Trade Commission statistics indicate that mergers are responsible for approximately twenty-two per cent of the total growth of these firms.

This recent surge of conglomerate acquisitions has attracted widespread public attention to the problems of conglomerate and aggregate concentration, and has stimulated a re-examination of the viability of federal antitrust merger law to deal with these problems. The purpose of this article is to explore the potential difficulties and attacks on conglomerate mergers by the Department of Justice combined to reduce the number of conglomerate mergers. See Bryan, supra note 1, at 32.


7. Conglomerate mergers often result in few economic efficiencies, particularly in pure conglomerate mergers where the product lines of the merging firms are unrelated. The opportunity for integration of production, research and development, or marketing and distribution functions is often extremely limited. Although improvement in management efficiency and ease of access to capital are potential benefits associated with conglomerate, studies have indicated that these benefits are seldom realized. On the other hand, the significant political and social consequences attributed to increased conglomerate and aggregate concentration include: the emergence of business corporations as a pre-eminent lobbying force in the American political process; the upset of the balance of power between labor and management; the disappearance of locally-owned enterprise; and limited opportunities for self-fulfillment through economic roles. See generally Bauer, supra note 1, at 234-36; Blake, Conglomerate Mergers and the Antitrust Laws, 73 Colum. L. Rev. 555, 557 (1973); Bryan, supra note 1, at 36-46; Mueller, The Effects of Conglomerate Mergers: A Survey of the Empirical Evidence, 1 J. of Banking & Finance 315, 317 (1977); Pertschuk and Davidson, supra note 4, at 13-17.


9. "Aggregate concentration" refers to the concentration of economic assets in general, without reference to concentration in any specific industry. See generally 1978 Hearings, supra note 3, at 44-46.

10. See 973 Antitrust & Trade Reg. Rep. (BNA) AA-3 (July 17, 1980).


usefulness of the theory of reciprocity as a basis for challenging conglomerate mergers under section seven of the Clayton Act.

This article will examine two opposing approaches to reciprocity, and will analyze each in terms of its usefulness in attacking conglomerate mergers. Additionally, alternative means of dealing directly with problems created by increased conglomeration and aggregate concentration will be discussed.

ANTITRUST LAWS APPLICABLE TO CONGLOMERATE Mergers

Current antitrust merger law focuses on the anticompetitive consequences of a conglomerate merger in a particular line of commerce and does not deal with the specific economic, social, and political ramifications associated with conglomerate mergers. Section 7 of the Clayton Act, as amended by the Celler-Kefauver Act in 1950, prohibits any merger, whether vertical, horizontal, or conglomerate in nature, if the effect of the merger may be to substantially lessen competition, or to tend to create a monopoly in any line of commerce. Conglomerate mergers may also be challenged by the Federal Trade Commission under section 5 of the Federal Trade Commission Act, which prohibits the use of unfair methods of competition.

Conglomerate mergers have been successfully challenged under Section 7 of the Clayton Act through the use of three theories: potential competition, entrenchment, and reciprocity. The potential competition doctrine focuses on the loss of procompetitive effects on the market had the acquiring firm entered the industry by means other than merger. The entrenchment theory deals with

13. Reciprocity is "the use of buying power to secure a competitive advantage in the sale of one's own products." See Von Kalinowski, 16 G. Business Organizations, Antitrust Laws and Trade Regulations § 63.01 (6th ed. 1979) [hereinafter cited as Von Kalinowski].


No corporation . . . shall acquire . . . the whole or any part of the stock . . . [or] any part of the assets of another corporation . . . 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.

15. See note 14 supra.


17. 15 U.S.C. § 45(a)(1) (1976) provides: "Unfair methods of competition in commerce, and unfair or deceptive acts or practices in commerce, are declared unlawful."

the danger to competition posed by the acquisition of a major competitor in the target industry and the possibility of the acquired firm using the extensive resources of the acquiring firm to "entrench" or augment its market position.\textsuperscript{19} Reciprocity theory deals with the anticompetitive effects which result from the use of a company's purchasing power to gain a competitive advantage in selling its products.\textsuperscript{20}

Until the early 1970's, conglomerate mergers were successfully challenged under each of these theories.\textsuperscript{21} Since that time, however, a trend has developed favoring defendants in conglomerate merger cases.\textsuperscript{22} Although consideration of the potential competition and entrenchment theories is beyond the scope of this article, it may generally be stated that problems of proof have rendered these theories ineffective in attacking conglomerate mergers.\textsuperscript{23} Although the theory of reciprocity has not been successfully employed in a conglomerate merger context since 1971,\textsuperscript{24} it may provide a viable basis for challenging conglomerate mergers in the future.\textsuperscript{25}

**The Theory of Reciprocity**

Reciprocity Defined

In its simplest form, reciprocity involves a company's use of its purchasing power to promote the sale of its own products.\textsuperscript{26} In a conglomerate merger context, the acquiring firm utilizes its sub-

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\textsuperscript{20} See notes 32-42 infra and accompanying text.

\textsuperscript{21} See Bauer, supra note 1, at 200-01, for a comprehensive list of successful and unsuccessful conglomerate merger challenges.

\textsuperscript{22} No conglomerate merger challenged under the federal antitrust laws has been declared illegal since 1974. See Bauer, supra note 1, at 200. The corresponding rise in the number of conglomerate mergers since the middle 1970's reflects, at least in part, this trend in conglomerate merger cases.

\textsuperscript{23} See generally Bauer, supra note 1, at 203-29; Bradley, supra note 18, at 1-5.

\textsuperscript{24} The last case in which a merger was successfully challenged on reciprocity grounds was United States v. White Consolidated Industries, Inc., 323 F. Supp. 1397 (N.D. Ohio 1971).

\textsuperscript{25} See text accompanying note 133 infra.

\textsuperscript{26} In United States v. General Dynamics Corp., 258 F. Supp. 36 (S.D.N.Y. 1969), the court described reciprocity as: "[T]he practice whereby a company, overtly or tacitly, agrees to conduct one or more aspects of its business so as to confer a benefit on the other party to the agreement; the consideration being the return promise in kind by the other party." Id. at 57.
stantial purchasing power to induce its suppliers to purchase from the acquired firm. Secondary reciprocity, another form of the business practice, occurs when a firm induces its suppliers to induce their suppliers to purchase from the firm’s affiliate.27

The term “reciprocity” embraces a variety of business relationships, which may be classified into three categories: coercive reciprocity, mutual reciprocity, and unilateral reciprocity. Coercive reciprocity involves the use of a threat by a purchaser to either withdraw purchase orders or withhold future purchases unless the supplier makes reciprocal purchases.28 Inherent in the practice is the exercise of economic leverage by a purchaser to exact reciprocal purchases from a disadvantaged supplier. Mutual or consensual reciprocity is a voluntary arrangement between two companies of relatively equal bargaining power.29 Although purchases by each firm are conditioned upon reciprocal purchases, threats are unnecessary because the relationship stems from the possibility of mutual benefit to both parties. Unilateral reciprocity occurs when, absent an agreement between the parties, a supplier voluntarily purchases from a firm to which it hopes to sell its own products.30 Because unilateral reciprocity is not technically a reciprocal practice in that a purchase by one party is not conditioned upon reciprocal purchases by the other, unilateral reciprocity is generally referred to as “reciprocity effect.”31

The Anticompetitive Effects of Reciprocal Dealings

Although there is substantial disagreement among economists as

28. See, e.g., FTC v. Consolidated Foods Corp., 380 U.S. 592 (1965), discussed at notes 49-73 infra and accompanying text. See also von Kalinowski, supra note 13, § 63.03(2); Finney, Reciprocity and Public Policy, 2 Antitrust Law & Econ. 97, 99 (1969) [hereinafter cited as Finney].
29. See United States v. General Dynamics Corp., 258 F. Supp. 36, 59 (S.D.N.Y. 1966), where the court stated that “mutual patronage” reciprocity occurs when both parties agree to purchase from one another even though they have equal purchasing power with respect to each other. See also von Kalinowski, supra note 15, § 63.03(2); Edwards, Conglomerate Bigness as a Source of Power, in Nat. Bur. Eco. Research, Business Concentration and Price Policy, 331 342 (1955); Flinn, Reciprocity and Related Topics Under the Sherman Act, 37 Antitrust L.J. 156, 158 (1969) [hereinafter cited as Flinn].
30. See von Kalinowski, supra note 13, § 63.03(2); Finney, supra note 35, at 99; Flinn, supra note 29, at 158; Hausman, Reciprocal Dealing and the Antitrust Laws, 77 Harv. L. Rev. 873, 877 (1964) [hereinafter cited as Hausman].
to the economic consequences of reciprocity, a number of anticompetitive effects have been identified by courts which have addressed the issue of reciprocity. First, the traditional economic decision-making criteria of price and quality are replaced at least in part by reciprocity considerations. This distortion of the competitive market selection process promotes inefficiency by allowing less competitive firms to prosper. The cost of this practice may ultimately be borne by the consumer in the form of higher prices or inferior products.

Second, significant barriers to entry are raised when reciprocal dealing is practiced. Under traditional economic theory, the threat of entry by new firms into the market stimulates competition among firms currently existing in the market. Firms without reciprocity power, however, are reluctant to enter a market when buyers in the market are engaged in reciprocal buying relationships with established market firms. Thus, the incentive to compete is effectively removed.

Finally, market foreclosure is considered the most significant anticompetitive effect of reciprocal purchasing. Conglomerates, which by definition are involved in diverse business operations, possess substantial purchasing power in many markets and thus are well-suited for reciprocal dealings. To the extent that reciprocity is practiced in a market by a conglomerate, single-unit or


34. The Supreme Court in FTC v. Consolidated Foods Corp., 380 U.S. 592 (1965) stated that: "The practice results in 'an irrelevant and alien factor.' ... F.T.C., p. ..., intruding into the choice among competing products, creating at the least 'a priority on the business at equal prices.' " Id. at 594. See also Hausman, supra note 30, at 879; Stocking & Mueller, Business Reciprocity and the Size of Firms, 30 J. Bus. U. Cm. 73, 85-88 (1957) [hereinafter cited as Stocking & Mueller]; Turner, supra note 1, at 1387.

35. See Hausman, supra note 30, at 879. See also Turner, supra note 1, at 1387.

36. See Hausman, supra note 30, at 879.

37. See Hausman, supra note 30, at 879. See also BAIN, BARRIERS TO NEW COMPETITION (1956) [hereinafter cited as BAIN].

38. See generally BAIN, supra note 37.

39. See von KALNOWSKI, supra note 13, § 63.05(1).

40. It has been suggested that: "[d]iversification not only increases the number of opportunities for reciprocal buying, it increases their magnitude." See Stocking & Mueller, supra note 34, at 77.
non-diversified firms which do not have reciprocity leverage will be foreclosed from that market.\textsuperscript{41} Diversified conglomerates are thus likely to flourish when reciprocity is practiced. As conglomerates prevail over competitors in the marketplace, aggregate concentration increases.\textsuperscript{42}

**Judicial Interpretation of Reciprocity**

The use of coercive reciprocity to promote sales was first condemned by the Federal Trade Commission in the 1930's.\textsuperscript{43} In *United States v. Griffith*,\textsuperscript{44} a 1948 case decided under the Sherman Act,\textsuperscript{45} the Supreme Court referred to the unacceptability of the practice of reciprocity when it is used to create a monopoly or to foreclose companies less favorably situated from the market.\textsuperscript{46} It was not until 1963, however, that reciprocity theories were first applied in a merger context. In *United States v. Ingersoll-Rand Co.*,\textsuperscript{47} the Third Circuit Court of Appeals declared that reciprocity was an anticompetitive practice which section 7 of the Clayton Act was intended to prohibit.\textsuperscript{48} Finally, in 1965, the Supreme Court dealt with reciprocity in a section 7 context in *FTC v. Consolidated Foods Corp.*,\textsuperscript{49} the Court's only treatment of the issue to date.

*FTC v. Consolidated Foods Corp.: The Supreme Court's Treatment of Reciprocity*

Consolidated Foods Corp., the owner of a network of wholesale and retail food stores, acquired Gentry, Inc., the second largest producer of dehydrated onion and garlic in a highly concentrated market.\textsuperscript{50} Consolidated Foods made substantial purchases from

\begin{itemize}
  \item 41. See von Kalinowski, supra note 13, § 63.05(1).
  \item 42. See Hausman, supra note 30, at 880.
  \item 43. See *In re Mechanical Manufacturing Co.*, 16 F.T.C. 67 (1932); *In re Waugh Equipment*, 15 F.T.C. 232 (1931). See also *In re California Packing Corp.* 25 F.T.C. 379 (1937). These actions were instituted pursuant to §5 of the Federal Trade Commission Act. See note 17 supra.
  \item 44. 334 U.S. 100 (1948).
  \item 47. 320 F.2d 509 (3d Cir. 1963). See notes 76-81 infra and accompanying text.
  \item 48. 320 F.2d at 524.
  \item 49. 380 U.S. 592 (1965).
  \item 50. Gentry, Inc., & Basic Vegetable Products, Inc., the leading industry producers, together accounted for 90% of the market, with each controlling, respectively, a 32% and 58% market share of total industry sales. Two other producers accounted for the remaining 10%.
\end{itemize}
food processors who in turn purchased dehydrated garlic and onions. This relationship created the opportunity for reciprocal dealings, and post-acquisition evidence revealed that Consolidated Foods did in fact engage in coercive reciprocity with food processors.

In *In Re Consolidated Foods Corp.* the Federal Trade Commission ruled that the merger violated section 7 of the Clayton Act. First, the Commission established that the merger increased the probability of reciprocal dealings in the garlic and onion industries. Two factors supported this finding: (1) an examination of the market structure revealed that the reciprocity power of Consolidated Foods and Gentry would be substantially increased by the merger; and (2) the fact that Consolidated Foods actually practiced reciprocity after the merger confirmed the finding that reciprocity power was created by the merger. The Commission further found that Gentry would have an unfair advantage over its principal competitor merely as a result of the connection with Consolidated Foods. The Commission concluded that when a merger created reciprocity power, the acquired firm would gain an unfair advantage through reciprocity effect, even if coercive or mutual reciprocity were not practiced.

Second, the Commission determined that the potential anticompetitive effects created by the merger were substantial. Evidence established that approximately twenty-five percent of all purchasers in both the garlic and onion industries were substantial suppliers of Consolidated Foods and thus subject to reciprocity pressures from that firm. The Commission further concluded that the merger violated section seven because it created the power to fore-

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51. *Id.* at 595.
52. *Id.* at 596-97.
54. Potential customers of Gentry were substantial suppliers of Consolidated Foods. *Id.* at 955.
55. *Id.*
56. *Id.*
57. The Commission found that Gentry could gain sales from processed food suppliers or prospective suppliers who would in turn hope that Consolidated Foods would reciprocate by purchasing processed food. *Id.*
58. *Id.* at 957. This finding was supported by the fact that Gentry, the acquired firm, already commanded a substantial share in an already concentrated market. The Commission concluded that any increase in sales within this two-firm oligopoly structure would only serve to enhance the noncompetitive nature of the industry and raise higher entry barriers into the market. *Id.* at 959.
close competition from a substantial share of the market, thereby creating a probability of a substantial lessening of competition in the dehydrated garlic and onion industries.

The Seventh Circuit Court of Appeals reversed the ruling of the Commission and approved the merger. The court concluded that post-acquisition evidence showed no substantial impact on the market, despite the efforts of Consolidated Foods to promote reciprocal dealings. Thus, a probability of substantial anticompetitive effect had not been established.

The Supreme Court reversed the decision of the Seventh Circuit, stating that the potential for reciprocity made possible by the merger was one of the "congeries of anticompetitive practices" against which the antitrust laws were intended to protect. The Court therefore declared that reciprocity constituted a violation of section 7 if a probability of substantial anticompetitive effect on the market in question could be established.

Examination by the Court of evidence of the market structure after the merger revealed that the merger created substantial opportunities for reciprocal dealing. The Court emphasized that post-acquisition evidence of actual reciprocal dealing and resulting changes in individual company market shares supported the Commission's ruling. The Court therefore held that the findings of the Federal

59. In this case, 25% was considered a substantial share of the market. Id. at 957.
60. See Consolidated Foods Corp. v. FTC, 329 F.2d 623 (7th Cir. 1964).
61. Post-acquisition evidence showed that Gentry's share of the dehydrated onion market increased by 7% while its share of the dehydrated garlic market decreased by 12%. Id. at 626.
62. Id. at 626-27.
64. Id. at 594. The Court further noted that reciprocal dealing may not result from "bludgeoning or coercion," but from more subtle arrangements, such as a threatened withdrawal of orders or a conditioning of future orders on reciprocal purchases. Id. Subsequently, in United States v. General Dynamics Corp., 258 F. Supp. 36 (S.D.N.Y. 1966), the district court stated that mutual reciprocity as well as coercive reciprocity was prohibited under §7 of the Clayton Act. Citing Consolidated Foods, the court reasoned that the Supreme Court implied that mutual reciprocity is as anticompetitive as coercive reciprocity. Id. at 58-59.
66. Id. at 600-01. It should be noted that the post-acquisition evidence was open to two interpretations. The fact that Gentry maintained its market position, even though it marketed an inferior product could imply that reciprocity had successfully maintained the company's market share. The Supreme Court accepted this interpretation of the evidence. The same evidence could also imply, however, that the reciprocal dealings had no substantial anticompetitive effect since Gentry's market share had not increased. The Court of Appeals based its decision on this interpretation of the evidence. See note 61 supra and accompanying text.
Trade Commission were supported by substantial evidence.

The Supreme Court's approval of the overall findings of the Commission may implicitly suggest that the Court approved the Commission's statements that the mere existence of reciprocity power is sufficient to establish a probability of a substantial lessening of competition. These statements by the Commission, however, were not essential to the Commission's findings or to the decision of the Court because Consolidated Foods actually engaged in reciprocity after the merger. The Court did not directly address the question of whether a merger which resulted in a market structure conducive to substantial reciprocal effect alone would create a probability of substantial anticompetitive effect.

Justice Stewart, in a concurring opinion, however, squarely confronted this issue. He stated that the mere opportunity for reciprocity was not sufficient by itself to invalidate a merger under section seven. Justice Stewart reasoned that to hold otherwise would effectively outlaw diversification because the possibility of reciprocal relationships is almost always created by conglomerate mergers. Justice Stewart further urged the Court to formulate standards of analysis for determining how effective reciprocity must be in order to invalidate a merger. In Justice Stewart's view, even actual reciprocity practices would not necessarily violate section 7 unless the probability of a significant alteration in the market structure can be established.

Justice Stewart's concurrence thus rejected the implication of the majority that the mere opportunity for reciprocity would be sufficient to establish a section seven violation. Further, he called for a "more closely textured economic analysis" to determine whether the effect of any reciprocal dealings would be substantially anticompetitive. Courts in subsequent reciprocity cases have either rejected Justice Stewart's view by holding that the mere opportunity for reciprocity is sufficient for a section 7 violation, or have embraced his views and developed a structural economic analysis of the probable effect of reciprocal dealings on the market in question.

67. Id. at 602.
68. Id. at 603.
69. Id. at 604.
70. Id.
71. Id. at 603.
72. See note 74-92 infra and accompanying text.
73. See notes 93-126 infra and accompanying text.
Reciprocity and Conglomerate Mergers

"Reciprocity Effect:" A Sufficient Basis to Establish Violation of Section Seven

A number of courts have adopted the position that the mere presence of reciprocity power, or reciprocity effect, may substantially affect competition. Under this approach, the existence of substantial purchasing power is held to induce hopeful suppliers of one of the merging companies to voluntarily purchase from the other merging company, thereby foreclosing suppliers with less reciprocity leverage from that market. As one court noted, when reciprocity leverage exists, a competitor will prevail only when its price is the lowest. There is no chance that when price and quality are equal, the "flip of the coin" will be resolved in favor of the competitor without leverage. The purchaser will always choose a supplier who may reciprocate.

The Third Circuit Court of Appeals, in United States v. Ingersoll-Rand Co., was the first court to adopt this approach. The case involved the attempted purchase of three leading producers of coal mining machinery by Ingersoll-Rand, a large manufacturer of industrial equipment. Ingersoll-Rand was a substantial purchaser of steel, and the steel manufacturers were in turn substantial purchasers of coal. The market structure after the merger was thus highly conducive to reciprocal dealings in that Ingersoll-Rand could coerce its steel suppliers to induce their coal suppliers to purchase from Ingersoll-Rand's newly acquired coal mining equipment manufacturers.

The mere existence of these possible reciprocal relationships was held to be sufficient grounds to uphold the issuance of a preliminary injunction. The court approved the district court's observation that Ingersoll-Rand need not consciously employ its reciprocity power to improve the market shares of its affiliates. The court reasoned that the mere existence of this purchasing power would alert the astute businessperson to the benefits of establishing a

75. Id. at 61.
76. 320 F.2d 509 (3d Cir. 1963).
77. The three leading coal mining machinery producers accounted for 60% of total market sales. Id. at 524.
78. Id.
79. This case is a classic example of secondary reciprocity. See note 27 supra and accompanying text.
80. 320 F.2d at 524.
favorable business relationship with Ingersoll-Rand.81

This liberal approach to reciprocity was also embraced by the Southern District Court of New York in United States v. General Dynamics Corp.82 The defendant, General Dynamics Corp., implemented a full-scale reciprocity program designed to reap all possible reciprocity benefits made possible by the merger. Thus, the court did not face the issue of whether reciprocity effect alone was sufficient to establish a section 7 violation. The court stated, however, that the mere presence of reciprocity power often leads to abuse and may operate to artificially stimulate sales, even absent overt utilization of the power.83 The court further stated that the anticompetitive consequences stemming from the presence of reciprocity power may be sufficiently serious to warrant diversiture.84

The Third Circuit Court of Appeals subsequently reaffirmed its Ingersoll-Rand position in Allis-Chalmers Mfg. Co. v. White Consolidated Indus., Inc.,85 a case factually similar to Ingersoll-Rand.86 The Third Circuit stated that a merger which creates a market structure conducive to reciprocal dealings is by itself anticompetitive.87 The court supported this position by a general reference only to the Supreme Court opinion in Consolidated Foods.88

Another court adopted a similar stance in a case factually related to Allis-Chalmers. In United States v. White Consolidated, Inc.,89 the District Court for the Northern District of Ohio stated that a substantial lessening of competition results when the market structure is conducive to reciprocity, regardless of the intention of the parties to actually engage in reciprocity.90 The sheer size of the

81. Id.
83. Id. at 58-9.
84. Id. at 67.
86. White Consolidated, a diversified manufacturer, attempted to acquire Allis-Chalmers, a manufacturer similar in size. Allis-Chalmers opposed the merger, in part on the basis of reciprocity. Because White Consolidated had already acquired Blaw-Knox Company, a leading manufacturer of rolling mills, the combined purchasing power of the merged company in steel mill products would be enormous. The merged firm could thus induce its steel mill products suppliers to induce their steel suppliers to purchase rolling fills from Blaw-Knox. The court did not consider the fact that reciprocal power already existed from the White Consolidated-Blaw-Knox affiliation. Id. at 519.
87. Id. at 518.
88. Id.
89. 323 F. Supp. 1397 (N.D. Ohio 1971). The case involved the merger of a sister firm, White Motor Corporation, with White Consolidated which would create a market structure similar to that found in Allis-Chalmers. See note 86 supra.
90. 323 F. Supp. at 1398.
parties in the market was considered by the court to "operate as a lever" to lessen competition. 91

Guidelines issued by the Department of Justice also reflect this view of reciprocity effect. 92 The Department of Justice employs a statistical approach to determine whether to challenge a conglomerate merger on the basis of reciprocity. A merger will be challenged for creating a significant danger of reciprocal buying when fifteen percent or more of the sales in any market where one of the merging firms sells are made by substantial suppliers of the other merging firm. The Department of Justice maintains that under these circumstances the opportunity for reciprocity after the merger is substantial and therefore sufficient to support a merger challenge.

"Reciprocity Effect:" An Insufficient Basis to Establish a Violation of Section Seven

The notion that a merger is illegal merely because it creates the opportunity for reciprocal dealings has been rejected in a second line of cases. As urged by Justice Stewart in Consolidated Foods, a "more closely textured economic analysis" has been developed to determine whether reciprocity will actually be practiced, and if so, whether it will have a substantial anticompetitive effect. For example, in United States v. Pennick & Ford, Ltd., 93 the District Court of New Jersey refused to invalidate a merger despite evidence that reciprocity activity was a common practice in the acquired firm's market. 94 The court focused on three factors which indicated that the merger did not create a probability of reciprocity which would have substantial anticompetitive effects. First, unlike a merger in an oligopolistic market setting, ten firms competed aggressively in the acquired firm's market. 95 Second, the fact that reciprocity was practiced to some degree in the industry before the proposed merger did not prevent a new entrant from becoming an industry leader. Thus, the relatively unconcentrated structure of the industry did not raise substantial barriers to market entry. 96 Finally, the

91. Id.
92. See Dept. of Justice Guidelines, 1 TRADE REG. REP. (CCH) 4510, at 6888.
94. Id. at 525-26.
95. See, e.g., FTC v. Consolidated Foods Corp., 380 U.S. 592 (1965), discussed at notes 49-73 supra and accompanying text.
96. 242 F.Supp. at 524.
97. Id.
acquiring company presented evidence of an anti-reciprocity policy, and the government failed to offer any evidence in rebuttal to suggest a departure from this policy. The court therefore concluded that reciprocal dealings were not likely to occur after the merger, and that in any event, no substantial anticompetitive effects were likely to result.

In *United States v. Northwest Industries, Inc.*, the District Court for the Northern District Illinois applied an even more restrictive approach to reciprocity. The court refused to invalidate a merger, even though it found that the merger would greatly increase the potential for reciprocity, and despite evidence that the customers and suppliers of both merging companies were engaging in reciprocity. In reaching its decision, the court focused on two factors which indicated that reciprocity would not actually be practiced after the merger. First, the acquired company's president testified that the company followed an unwritten anti-reciprocity policy. Second, the acquiring company, a diversified conglomerate, treated each subsidiary as a separate profit center, with each manager having a financial stake in the profits of the subsidiary. Based on these two factors, the court concluded that it was impossible to determine whether reciprocity would actually be practiced.

The "more closely textured economic analysis," advocated by Justice Stewart in *Consolidated Foods* and applied by the courts in *Penick & Ford* and *Northwest Industries*, took the form of an analysis addressing the particular facts involved and emphasizing such factors as anti-reciprocity policy, more competitive market structures, and ineffective past reciprocal dealings. An even more comprehensive analytical framework was later set forth by two courts, the District Court of Connecticut and the Northern District Court of Illinois, in three decisions involving merger challenges to which International Telephone & Telegraph Corp. (ITT) was a party: *United States v. ITT (Grinnell and Hartford)*; *United

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98. *Id.* at 525.
99. *Id.*
100. 301 F. Supp. 1066 (N.D. Ill. 1969).
101. *Id.* at 1088.
102. *Id.* at 1088-89.
103. *Id.* at 1091-92.
104. *Id.* at 1092.
105. See note 71 *supra* and accompanying text.
106. 306 F. Supp. 766 (D. Conn. 1969) (action for preliminary injunction of mergers be-
A two-step analysis was applied in all three decisions to determine whether the merger would result in a substantial lessening of competition because of the reciprocal dealings made possible by the merger. First, it must be determined whether the market structure after the merger will create an opportunity for reciprocal dealing. A careful analysis of the following factors is required to make this complex determination: (1) the extent to which suppliers of the acquired firm are actual or potential purchasers of the acquired firm's products; (2) whether the acquired firm's business has characteristics which encourage reciprocal dealings; (3) the scope of the market represented by the acquiring company for products sold by its suppliers; (4) the size and diversification of other companies to which the acquired suppliers sell their products; and (5) the degree to which the markets within which the suppliers operate are competitively structured.
If a market structure conducive to reciprocal dealings can be established, the next step of the analysis is to assess the likelihood that reciprocity will in fact occur.\(^\text{115}\) Factors to be considered in making this determination include: (1) a firm's adherence to an anti-reciprocity policy;\(^\text{116}\) (2) the existence of individual profit centers;\(^\text{117}\) (3) a firm's failure to gather data necessary to identify reciprocity opportunities;\(^\text{118}\) and (4) the fact that the merging companies have not engaged in or benefited from past reciprocal dealings in the industry.\(^\text{119}\) The District Court of Connecticut concluded that when the first three factors are present, reciprocity would not be likely to occur, even if a market structure conducive to reciprocal dealing was created by the merger.\(^\text{120}\) Similarly, the Northern District Court of Illinois concluded that, when all four factors are present, adequate safeguards against any significant practice of reciprocal dealings would be demonstrated.\(^\text{121}\)

The Northern District Court of Illinois added a third step to the above analysis by further determining whether those reciprocal dealings, if proven likely to occur, would have substantial anticompetitive effects.\(^\text{122}\) The court did not discuss this third element in detail because the plaintiff failed to meet the second requirement of establishing a likelihood of reciprocal dealings. In *United States v. General Dynamics Corp.*,\(^\text{123}\) however, the Southern District

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\(^\text{115}\) *See*, U.S. v. ITT (Canteen), 1971 Trade Cas. 73,619, at 90,545 (N.D. Ill. 1971); U.S. v. ITT (Grinnell), 324 F. Supp. 19, 42 (D. Conn. 1970).

\(^\text{116}\) In the Grinnell merger, the court noted that ITT had a written antireciprocity policy which was widely disseminated on a continuing basis since 1966. 324 F. Supp. at 46. In the Canteen merger, the court also emphasized the long-standing antireciprocity policy of ITT. 1971 Trade Cas. at 90,552. The existence of antireciprocity policies was also essential to the decisions in *United States v. Penick & Ford, Ltd.*, 224 F. Supp. 518 (D.N.J. 1965), discussed at notes 93-99 *supra* and accompanying text, and *United States v. Northwest Industries, Inc.*, 304 F. Supp. 1066 (N.D. Ill. 1969), discussed at notes 100-104 *supra* and accompanying text, even though there was no evidence that these policies were actively promoted. *See* notes 98 and 103 *supra* and accompanying text.

\(^\text{117}\) The profit center organization of ITT was significant in all three merger decisions for a determination that reciprocity was not in fact likely to occur. *See* U.S. v. ITT (Canteen), 1971 Trade Cas. 73,619 at 90,552 (N.D. Ill. 1971); U.S. v. ITT (Grinnell), 324 F. Supp. 19, 46 (D. Conn. 1970); U.S. v. ITT (Grinnell and Hartford), 306 F. Supp. 766, 782-83, 790 (D. Conn. 1969). The court in *United States v. Northwest Industries, Inc.*, 301 F. Supp. 1066 (N.D. Ill. 1969), discussed at notes 100-104 *supra* and accompanying text, also emphasized this factor. *See* note 104 *supra* and accompanying text.

\(^\text{118}\) 1971 Trade Cas. at 90,552; 324 F. Supp. at 44-45.

\(^\text{119}\) 1971 Trade Cas. at 90,551; 324 F. Supp. at 43.

\(^\text{120}\) 306 F. Supp. at 783, 790.

\(^\text{121}\) 1971 Trade Cas. at 90,552-53.

\(^\text{122}\) 1971 Trade Cas. at 90,544.

Court of New York adopted a similar three-step analysis and provided more specific guidance for determining when reciprocal dealings will have substantial anticompetitive effects. The court stated that a threshold determination must be made of the amount of market foreclosure which can be expected to occur as a result of the defendant's activities. Next, it must be determined whether this amount of foreclosure is sufficient to substantially lessen competition. The percent of foreclosure necessary for a substantial lessening of competition should then depend on the concentration level of the industry.

**The Future Viability of the Theory of Reciprocity in Attacking Conglomerate Mergers**

**Current State of the Law**

The *Penick & Ford*, *Northwest Industries*, and *ITT* cases reflect a reluctance on the part of courts to find a probability of substantial anticompetitive effects resulting from reciprocal dealings. In *Northwest Industries*, the court refused to find a probability that reciprocity would be practiced, despite evidence which showed that reciprocity was being practiced by both Northwest Industries and B. F. Goodrich and their customers and suppliers. Although the court acknowledged the anticompetitive effects engendered by reciprocity as well as the reciprocity leverage created by the challenged merger, the court justified its decision on two questionable evidentiary grounds which allegedly discouraged reciprocal dealings: an unwritten anti-reciprocity policy and the existence of independent profit centers. The court did not, however, question the effectiveness of a company policy against reciprocity which was never reduced to writing. Moreover, no evidence was offered to indicate that this policy was actively promoted in any way throughout the company. Further, the court ignored the possibility that even though each subsidiary operated as an independent profit

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124. 258 F. Supp. at 63. An approximation of this amount may be made by determining: (1) the amount of sales made to major suppliers who are able to reciprocate; and (2) the percentage of the acquired firm's market this figure represents. *Id.*
125. *Id.* at 64.
126. Because of the highly concentrated nature of the industry, a predicted market foreclosure figure as marginal as 1.3% was found sufficient to sustain the challenge to the merger. *Id.*
127. *See* note 102 *supra* and accompanying text.
128. *See* notes 101-102 *supra* and accompanying text.
129. *See* notes 103-104 *supra* and accompanying text.
center, profit center managers might collaborate to establish a reciprocity policy beneficial to all. The decision in *Penick & Ford* also suggests that, even though reciprocity may commonly be practiced in the relevant markets of the merging companies or by the companies themselves, evidence demonstrating such facts will not necessarily establish a probability that reciprocity will be engaged in after the merger.\(^{130}\)

Finally, the *ITT* cases fully incorporate the significant factors considered in *Penick & Ford* and *Northwest Industries*. These cases indicate that even if a market structure highly conducive to reciprocal dealing is created by the merger, the merger will not necessarily be deemed illegal if the merging companies appear to adhere to an anti-reciprocity policy or are structurally organized into independent profit centers.\(^{131}\) Thus, it seems possible that a challenge to a merger predicated on the theory of reciprocity may be defeated if the merging companies at least appear to adopt a policy designed to prevent reciprocal dealings.\(^{132}\)

Nonetheless, reciprocity may still serve as a viable substantive tool for challenging conglomerate mergers if courts in the future adopt the view that a merger which creates the opportunity for substantial reciprocal dealings violates section seven of the Clayton Act. The *Ingersoll-Rand* line of cases provides strong support for courts willing to adopt this theory as a means of halting the trend toward increased conglomeration. A reciprocity effect analysis, which does not require the detailed projection of expected reciprocity practices embodied in the *ITT* analysis, imposes a substantially lighter burden of proof. Once it is established that the merger creates a market structure conducive to reciprocity, it is presumed under the reciprocity effect theory that the resulting anti-competitive effects will be substantial. Thus, particularly in light of the current ineffectiveness of other substantive grounds sought to support a conglomerate merger challenge,\(^{133}\) the reciprocity effect theory may provide the most viable avenue for control-

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130. See notes 94-99 supra and accompanying text.

131. See notes 115-121 supra and accompanying text.

132. Although the operation of trade relations departments which openly engaged in reciprocity was a common practice of conglomerate firms until 1965, as corporations became aware of the illegality of this business practice, trade relations departments were eliminated and anti-reciprocity policies were at least nominally adopted. Thus, it would appear that most corporations would now be able to successfully defend a merger challenge predicated on reciprocity grounds in courts which adopt the *ITT* approach.

133. See note 23 supra and accompanying text.
Reciprocity and Conglomerate Mergers

Reciprocity and Conglomerate Mergers

The Federal Trade Commission and the Department of Justice in the recent past have expressed interest in pursuing the theory of reciprocity as a basis for challenging conglomerate mergers. The Federal Trade Commission has been seeking test cases to challenge conglomerate mergers under section 5 of the Federal Trade Commission Act. The FTC expressed interest in the use of reciprocity as a basis for conglomerate merger challenges. In October, 1978, the Department of Justice filed an action against United Technologies Corporation. The action was consolidated with a private action previously instituted by Carrier Corporation to block a tender offer and takeover bid by United Technologies. Both Carrier Corporation and the government challenged the proposed tender offer on the basis of entrenchment, reciprocity, and horizontal and vertical competition theories. In a preliminary injunction proceeding, in which the injunction was denied, the Northern District Court of New York applied the three-step \textit{ITT} analysis to the reciprocity claim.

The court examined the anti-reciprocity policies of the defendant to determine the probability of future reciprocal dealings. The court suggested that, although United Technologies had a written policy against reciprocity, the proffered evidence cast doubt upon the extent to which these written policies were disseminated and carried out. Noting that some instances of reciprocal dealing had occurred, the court stated that further discovery might reveal more widespread reciprocal practices and that the questions involved were of sufficient significance to warrant a trial on the merits. Significantly, the court looked beyond the surface of anti-reciprocity policies and suggested inquiry into their effectiveness. The possibility of feigned anti-reciprocity policies operating suc-

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134. 848 \textit{Antitrust & Trade Reg. Rep.} (BNA) AA-1-2 (Jan. 26, 1979) (Statement of Bureau Director Dougherty); 873 \textit{Antitrust & Trade Reg. Rep.} (BNA) AA-3 (July 20, 1978) (Statement of Chairman Pertschuk).
137. \textit{Id.}
138. \textit{Id.} at 76,361.
139. \textit{Id.} at 76,371.
140. \textit{Id.} at 76,372.
cessfully as a defense will be reduced if other jurisdictions follow the lead of the court in *United Technologies* by carefully scrutinizing evidence of this defense.

**The Need for Legislation**

The renewed interest of the Department of Justice and the Federal Trade Commission in using reciprocity as a basis for attacking conglomerate mergers is in response to a growing concern over the trend toward conglomerations and aggregate economic concentration developing during the past twenty years. The current surge of conglomerate acquisitions has highlighted this concern. Attention has centered specifically on the economic, political, and social consequences of increased conglomeration and economic concentration.141

Section seven of the Clayton Act, however, does not focus on these problems. Rather, section 7 addresses the anticompetitive effects of a merger in a particular line of commerce. The analysis which has developed under the reciprocity theory is aimed at preventing undue concentration in any particular industry. As a result, reciprocity may not be suitable for attacking the problem of increased aggregated concentration. New legislation is needed which deals directly with these problems.

Several legislative proposals prohibit conglomerate mergers on the basis of the size of the merging entities. One such proposal, incorporated into the Kennedy-Metzenbaum bill,142 generally prohibits mergers if the assets or sales of one of the merging entities exceed a specified amount. Such acquisitions are permitted, however, if positive societal benefits from the merger can be demonstrated. An alternative proposal by the Federal Trade Commission embodies a “cap and spin-off” approach,143 which would permit acquisitions by large firms only if accompanied by the divestiture of other viable entities equivalent in size to the acquired firm.144 Both of these proposals would accomplish the goal of halting the current conglomerate merger movement and the growing trend toward increased aggregate concentration.

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141. *See* note 7 supra.
144. *See* Pertschuk and Davidson, *supra* note 4, at 17-18.
CONCLUSION

The current merger movement has sparked renewed interest in reciprocity as a basis for conglomerate merger challenges under section 7 of the Clayton Act. Although the theory has not been successfully employed for that purpose since 1971, the theory may still be viable. Courts following the ITT approach are unlikely to find that reciprocity is a sufficient basis for establishing a section seven violation. However, if courts were to adopt the Ingersoll-Rand approach that a merger may violate section 7 if it creates the opportunity for reciprocal dealings, there is chance for success in challenging anticompetitive conglomerate mergers. Because reciprocity theories are aimed at preventing concentration in a particular line of commerce and not in the economy as a whole, new legislation which directly confronts the problems caused by increased conglomerate and aggregate concentration must be adopted. Only through the revitalization of the reciprocity theory or other theories applicable to conglomerate mergers under section 7, or through the enactment of new legislation, can the anticompetitive effects of conglomerate mergers be controlled.

CAROL A. DOYLE