ANTITRUST - A ROUTE TO CENTRALIZED GOVERNMENTAL PLANNING?

by Luther McKinney

It is popular to contend that bold new antitrust theories will eliminate numerous social problems. So it is we are witnessing a flood of proposals to cure inflation, unemployment, productivity shortfalls, advertising abuses, nutritional deficiencies, industrial concentration, and almost every conceivable economic difficulty.[1] Unquestioning application and testing of these patent-medicine claims in the food industry are leading, in my opinion, to counter-productive, centralized governmental planning in the guise of anti-trust policy. Hence, I would urge every American to critically consider the merits of emerging antitrust policy rather than accept it at face value.

Antitrust policy has historically developed as a unique mixture of politics, economics and law. Over an 86-year period, Congress has generally legislated a national economic policy of free competition. Economists have joined in an attempt to define a concept of free competition worthy of achievement. Lawyers, as advocates and judges, have engaged in a case-by-case interpretation of these laws and theories.

The policy originated in 1890 with the Sherman Antitrust Act, which requires each firm to make its business decisions inde-pendently and to avoid monopolization or attempts to monopolize.[2] Next, Congress, in response to claims that the Sherman Act was too vague,[3] enacted the Federal Trade Commission Act[4] outlawing "unfair methods of competition," and also passed the Clayton Antitrust Act[5]

Invited paper, AAEA annual meetings, Penn State University, Aug. 15-18, 1976

prohibiting, among other things, acquisitions and price discrimination that may substantially lessen competition or tend to create a monopoly.

In 1936, the Clayton Act was amended by an anti-chain store bill known as the Robinson-Patman Act to more specifically prohibit discriminations in price, service, or facilities, in an effort to stop concessions demanded of food suppliers by large chain stores.[5A] In 1938, the Federal Trade Commission Act was amended to prohibit deceptive acts and practices.[6]

Any objective ranking of these acts in terms of ability to preserve the fundamental aspects of competition affecting both the competitor and the consumer would rank the Sherman Act prohibitions against price fixing and other per se illegal restraints of trade in first place by a wide margin. The Sherman Act prohibitions against illegally obtaining or maintaining the market power to control prices or exclude competitors have been effective as well, but time-consuming to enforce, due to the complex economic issues involved.

The remainder of what is popularly regarded as American antitrust legislation reads well on paper, but is the subject of mixed reviews from a practical standpoint. Theoretically, an anti-merger statute intended to nip incipient monopolies in the bud is difficult to criticize. Likewise, the concept of preventing discrimination or the inducement thereof when it is destructive of competition is appealing. The problem has been one of application. All too often such legislation has been viewed as a tool to maintain the status quo in the face of inevitable and desirable change.

The Clayton, Federal Trade Commission, and Robinson-Patman Acts are all based on the idea that public interest will be best served by preserving many small firms operating in a purely competitive market.[7] Obviously, that policy has not been literally enforced, or we would all be associated with World War I horse and buggy industries instead of a modern, international marketplace requiring economies of scale to survive.

A realistic compromise between theory and practial reality has resulted from a strenuous adversary process. For example, countless antitrust enforcement resources were expended over many years out of fear that the rapid development of a more efficient food distribution system would destroy small food retailers.[8] Nevertheless, the trend to modern methods prevailed. Efficient small stores offering convenience survived, and the facts clearly establish that the consumer is significantly benefited where scale economies accrue.[9] Indeed, members of the federal agencies who fought this delaying action now admit that in the food industry "divestiture or deconcentration . . . could well raise prices and injure consumer welfare."[10*]

In spite of the inconsistencies between theory and reality,

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* Enforcement of the Robinson-Patman Act provides countless illustrations. For instance, food retailers, over the years, who operated truck fleets were forced to run empty on return trips because the FTC viewed back-haul allowances by suppliers as disriminatory. While this area of policy is still murky, pressure to improve productivity has forced the agency to begin clarifying its position on the subject. (FTC Advisory Opinion, Digest No. 147 (Oct. 23, 1967) and subsequent clarification; 3 Trade Reg. Rep. ¶18089 at 20537-20538, ¶20498, ¶20850, ¶21021).

a gradual give-and-take, case-by-case interpretation of the four underlying statutes resulted in evolutionary changes that had no crippling or shock-effect on business generally, since there was sufficient time and opportunity to present opposing views and to adjust to policy shifts.

The regulators, however, were not totally satisfied with that approach. They desired a more immediate involvement in business decisions. Businessmen provided an escape for the administrators by demanding more certainty regarding the applicability of antitrust policy. Consequently, the issuance of government guidelines became popular.* FTC Trade Regulation Rules, with binding legal effect, cover numerous areas.[11] Recently, in a further effort to avoid case-by-case interpretations, the Federal Trade Commission sought and secured legislation providing that a cease and desist order against one industry member will subject other industry members to a $10,000 per day penalty, providing they had notice of the order and engaged in acts that would be a violation of such order.[12]

The result has been to arm the regulators with strong procedural devices to minimize the role of the historical adversary system of policy evolution. Since the penalties for violation are so immense, many business people fear incurring the wrath of these regulatory

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* For example, the FTC issued restrictive trade rules governing prospective mergers in the dairy industry. (38 Fed. Reg. 17770 (1973); 1 CCH Trade Reg. Rep. ¶4532). In the case of grocery manufacturing firms, the Federal Trade Commission promulgated rules regulating proposed mergers (1 CCH Trade Reg. Rep. ¶4430). Similarly, the Justice Department issued merger guidelines (1 CCH Trade Reg. Rep. ¶4510).

czars. As a result, desirable changes in market structure, dictated by changing circumstances, may be slowed substantially to the possible detriment of consumer welfare. Still, our business system has been sufficiently strong to endure. I suspect that change can still occur as needed, even under the guidelines approach to antitrust policy, to permit continuation of the efficient system we have come to expect.

I cannot say the same for the move now afoot to establish the next generation of antitrust policy. Reduced to its lowest common denominator, that policy would allow the government to restructure, through divestiture orders, any industry deemed to be too concentrated. Current examples of the FTC's attempts to create such a policy include suits against the four largest ready-to-eat cereal manufacturers[13] and the eight largest oil marketers in the U.S.[14] for so-called "shared monopolies." If these proposals succeed, they will outlaw the market structures of about one-third of U.S. industry.[15*] I believe that the shock of such a change would be too great for our business community to absorb without some unpleasant effects.

The FTC's assault in the cereal case goes to the very heart of numerous segments of the food industry where many companies find themselves among the top four to eight firms accounting for more than half of a segment's sales.[16]

In 1972, the Federal Trade Commission charged that Kellogg, General Mills, General Foods, and Quaker were participating in a

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* Publicity indicates that the recently announced investigation of the automobile industry is based on this same emerging policy (Wall Street Journal, (Aug. 4, 1976); New York Times, p. 1 (Aug. 4, 1976); Chicago Tribune, Sec. 4, p. 9 (Aug. 4, 1976)).

"shared monopoly" of the ready-to-eat (RTE) cereal industry. The charges were said to be justified, based on the limited number of firms in the business and their aggregate market share -- an approach that had no prior basis in either legislation or case law. A few of the facts of this case may serve to illustrate the "wonderland" philosophy associated with this type of antitrust policy.

In June, 1969, Rufus E. Wilson, then Chief of the Division of General Trade Restraints at the FTC, in an internal memorandum suggested that an RTE case be instituted on the basis that the industry was a "non-competitive" business "with a three-firm market share of 83%, with entry virtually barricaded by these three firms . . ." He referred to the "controlling oligopoly" as including Kellogg, General Mills, General Foods, but not Quaker.[17]

In view of that background, the naming of Quaker as a respondent, along with the top three firms in the business, came as a surprise. Facts adduced in the trial have not cleared up the confusion. These facts show that Quaker's share of sales has never exceeded 10% of the business, and that for the 26 years preceding 1970, Quaker's average share of the RTE business was 4%, compared to the aggregate share of 82% enjoyed by the three largest firms.[18] For 31 of the 35 years preceding the 1972 complaint, Quaker was not even among the top four firms.[19] In fact, Quaker only achieved fourth position in 1968, moving from sixth position where its share of the business for years had been in the magnitude of 2% to 4%.[20] Interestingly, Nabisco, which was not named a respondent, averaged 9% of the business from 1937 to 1970 compared to Quaker's 3.8%.[21]

While we may never learn precisely what the Commission hoped to gain by involving Quaker, it seems apparent that we were included because of our successful competition against the rest of the industry in the mid 1960's -- since before then our share had been only in the 2% to 3% range. You might say we are being penalized for competing vigorously with the three industry leaders -- moving from a modest RTE business to the fourth-ranking position in the industry. Is the FTC now saying that internal growth by a small competitor to a fourth-place position warrants suit? Is that an unbending, bureaucratic dedication to a four-firm concentration ratio? If so, there is clearly a point where a company should stop competing, because of the new risk that a government bureaucracy may decide that success has made it part of a "shared monopoly."

The remedies the FTC seeks from Quaker are limited and contradictory to the basic charges of the complaint. It wants to prohibit us from making any acquisitions in the RTE cereal area for the next 20 years.[22] Quaker has not acquired a cereal business in the last 50 years,[23] and has no present plans of doing so.

The only other relief requested from Quaker is the prohibition of its shelf-space programs designed to assist retail grocers in managing displays of RTE cereal in their stores.[24] But the thrust of the complaint on this subject is that Quaker did not push its shelf-space program hard enough in competition with the program offered by Kellogg.[25] The FTC staff would, therefore, ban that which the complaint claims Quaker should have promoted aggressively. This is contradictory.

Much more is sought from the three industry leaders (Kellogg, General Mills, and General Foods), including a sweeping restructuring of their businesses, extensive trademark licensing, and a redistribution of some top-selling brands. The FTC staff wants three new companies spun out of Kellogg, asking that Kellogg give up its Rice Krispies and Special K brands, along with manufacturing facilities and other unnamed labels, to get the new companies started. General Mills would have to spin off one new company and give it a plant and the Wheaties brand, while General Foods would also have to spin off one new company and give it a brand as yet unspecified.[26]

The foremost pressure on federal officials to take an anti-big business stand and bring this type of case is to be found in an overly simplistic ideal called "atomistic competition." Since the late 19th century, orators in the political arena have proclaimed over and over that the strongest economy is one involving many small business units operating in a purely competitive marketplace.[27] This belief has permeated our thinking as a principle of the first order. It has become a political and social ideal. But the principle is, as many leading economists have noted, "self-deceptive" because "competition so conceived has never existed in any economy and, in fact, could not exist."[28] A well-intentioned minority in the academic community has embraced that self-deceptive illusion as the cornerstone of a move to fragment American industry. This illusion built up steam with the claims of depression economists that concentrated industries were extracting supra-competitive profits.[29] It was encased in a shiny veneer in the 1960's by industrial organization economists who claimed that industry performance is dictated by industry structure.[30] Thus, the apparent solution looked simple--atomize an industry, and better performance will flow.

In that connection, it is appropriate to repeat Harry Truman's belief that "If you laid all the economists in the U.S. in a straight line, they'd point in all directions."[31] The truth is that the structural view is not fully established, even in industrial organization economics.[32] Unfortunately, "trust-busting" claims receive prominence, and informed explanations to the contrary are often ignored. Consequently, a theory, unsupported by empirical evidence and still being hotly debated among economists, has been adopted by the FTC as the basis of a radical change in antitrust policy.

None of the four major U.S. antitrust statutes decrees that an industry may be dismantled solely because some arbitrary, aggregate level of concentration is reached. This past June, Thomas Kauper, recently Assistant U.S. Attorney General in charge of the Antitrust Division, stated that he did not believe that Congress had yet delegated this role.[33] The Justice Department has dropped a "shared monopoly" case against tire manufacturers.[34] Nevertheless, the Federal Trade Commission is assuming a regulatory role, similar to that of the Interstate Commerce Commission, in which it would judge the structure and performance of an industry as if it were a public utility,* and then reorganize and regulate the industry in order to

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* For example, individual firm rates of return on capital employed will be acceptable to the regulators only if they compare favorably with the average rate of return of all manufacturing firms in the U.S. In re Kellogg, et al., Docket No. 8883.

improve its performance. It is doing so despite Congressional deliberations during which there was expressed a total opposition to the establishment of any trade commission that would be authorized to regulate industry generally as if it were a public utility.[35]

Current Congressional activity demonstrates that Congress does not feel it has delegated such authority to the FTC. If the FTC has the power to restructure industries under existing laws, why are members of Congress presently debating the merits of anti-concentration bills to accomplish this very objective? Very recent examples are the Hart-Scott Antitrust Bill[36] and Indiana Senator Birch Bayh's bill to break up vertical integration in the country's 18 largest oil companies by dividing them into separate firms engaging only in production, refining, pipelines, or marketing.[37] If Congress believed that federal officials already possessed this power, why bother?

In my view, the Agency is being goaded into continuing the pursuit of these doubtful horizons by a proliferation of the works of popular writers who characterize the profit-maximizing goal of business as cold-hearted. William Robbins, in his book <u>The American Food Scandal</u>,[38] charged the four largest cereal producers with "profiteering" and the food industry, in general, with lying to the American people about the true price and quality relationship of their food. Speaking for Quaker, these charges are false. The point is, however, that these books have a strong, immediate, political impact, even when inaccurate. Through emotional appeals, they cause fear and confusion. This leads to demands for someone to act. Federal officials react under such pressure and are so doing despite the consequences.

Before this process carves the new policy in stone, I sincerely hope that someone in a position to be heard will cry out with the truth that federal reorganization of industry is necessarily based on a false assumption. That assumption is that non-elected, transitory government officials have the wisdom, despite a general lack of business experience, to more properly structure an industry than the vast combination of economic forces bearing on the market.

The public should be informed that the U.S. is, by this policy, moving into a new era of central economic planning. Frightening questions arise: Who in the federal government will fill this god-like role of reorganization? Who will determine which firms deserve what share of each industry after deconcentration? If after reorganization some firms, through competition, enlarge their market shares, will another round of reorganization be required, and, if so, how often?

Have federal bureaucracies previously demonstrated such high competence and skill in coordinating lesser tasks that they deserve our faith with such a monumental responsibility and undertaking? Were you satisfied with their performance during price controls? Did the effects of the Russian wheat deal meet with your approval? Have you been impressed with regulated industries such as railroads controlled by the ICC? Has the postal service been up to your expectations? Have you been impressed with the government's management of our Social Security fund? Since bureaucratic rules may often be perpetuated to insure job security for the regulators themselves, can we be sure that they are a tolerable substitute for the impartial laws of supply and demand?

For business people, the best indicator of growth of the federal government is the number of new regulations that continually pour out of Washington. Before they can become official, all regulations must be published in the Federal Register. When it was first published in 1936, the Register had 2,411 pages. By 1974, it had grown to 45,422 pages. Last year it grew to an astronomical 64,000 pages--growth of 42% from the previous year. One source likened the massive document to the most monumental book since Gutenberg's Bible! It is estimated that each American family pays $2,000 per year (at least one year's supply of groceries) to support this and other aspects of the federal bureaucracy.[39]

This movement to fragmentize and sterilize domestic firms comes at an odd moment in our economic history. With the passing of the stable international economic system established at the end of World War II, so passed America's ability to remain isolated. Americans cannot afford to be overly protective of economic ideals other than those capable of satisfactory performance in both domestic and international marketplaces.

Given the worldwide, intensive competition for scarce resources, "bigness" in American business may finally be coming into an age when it may, by necessity, be "goodness" in critical economic areas. The federal government, however, has limited its economic focus to domestic market protection via its emerging antitrust policy, with seemingly little concern for the international implications.

The four laws that make up our national economic antitrust policy were framed and passed when development of the national marketplace greatly overshadowed international trade in economic importance. The periods surrounding 1890, 1914, and 1936 were times of political isolationism as well as strong grass-roots discontent with domestic economic conditions. Rather than now using these laws to dismantle our business system, it seems more appropriate to consider whether these acts remain valid in the present era when international economic considerations must rank equally with domestic priorities in order to assure that the U.S. retain its competitive position in world markets? Shouldn't we be looking to secure entrepreneurial opportunity within the context of a strong, private enterprise system rather than embark on a project of destroying our business structure in favor of a giant bureaucracy?

The fact of the matter is that concentration of business in the U.S. is lower than in other major countries in the world.[40] In the Soviet Union, concentration is a fundamental principle of that nation's centrally planned economy. Thus, in terms of international trade, the strokes of our antitrust law brush may be painting us into a very tight corner.

Additionally, I am curious as to how the regulators will stimulate the innovation required to discover substitutes for dwindling supplies of necessary resources, improve productivity, and increase consumer satisfaction. Structural remedies, as sought by the FTC in the RTE cereal case, could effectively stagnate a target industry. Innovation normally flows from experimentation and risk-taking, spurred on by the profit motive. Whether firms will invest in R&D and take risks to produce major innovations is an open question if, upon success in the marketplace, they will be told to divest the successful assets or license trademarks, royalty-free, so that others may capitalize on their hard-won goodwill and success.

It was alarming to learn that the cereal business was selected as a test case because it was viewed as having less political clout than others.[41] This implies a desire by some regulators to quietly establish this controversial policy without risking political and public debate. The real problem with such a low profile is that it masks an attempt to withhold freedom of choice from American consumers. It seems some federal regulators have concluded that consumers buy too many varieties of ready-to-eat cereals. The trademark licensing remedy in the cereal case is designed to discourage development of further varieties. Yet, Americans have jealously guarded their constitutionally protected freedom of choice in other areas. Why would we surrender this freedom to government officials in deciding what food products we will consume (so long as there is no health or safety hazard)? How long will our freedom of choice last elsewhere if we let federal officials assume they have the right to absorb it in this instance? An individual's economic, social, and political choices are interwoven and not easily separable. Restriction of one must have substantial effects on the others. How safe are our freedoms of speech and press when the economic forum, of which they are parts, is to become the realm of the government regulator?

In Orwell's prophetic work 1984,[42] he portrayed a society where reality was the opposite of the image painted by the government. The Ministry of Love in that novel controlled the minds of citizens through terrifying uses of fear. Similar contradictions are present in the federal government's move against our private market structures. It declares that concentration in business must be reduced through concentrated, centralized government planning. If we accept this panacea, we may learn to our detriment the truth of Orwell's view that the inherent nature of all highly centralized governmental organizations is to suppress that which they profess to protect.

Many agree with the editors of Fortune magazine who recently warned that the "real danger to American liberty is not that it will be trampled by iron heels but that it will be slowly buried in a dust of bureaucratic oppression. . . We will have to insist, as a start, that legislators be much more cautious about authorizing government agencies to do things--and much more diligent about specifying what they may not do."[43]

NOTES

1. S. 1284, 94th Cong., 1st Sess. (1975) (i.e., Hart-Scott Antitrust Bill); H.R. 8532, 94th Cong., 2d Sess. (1975) (Rodino Antitrust Bill); S. 2387, 94th Cong. 2d Sess. (1976) (Bayh oil deconcentration bill); H.R. 9182, 94th Cong., 2d Sess. (1976) (Food Industry Reports Act). Complaint, In re Kellogg FTC Dkt. #8883, 3 Trade Reg. Rep. ¶20388 at 20269-20271 (July 17, 1973).

2. 15 USC §2 (Sherman Act).

3. Henderson, The Federal Trade Commission, 127, p. 4; S. Rep. 597, 63rd Cong., 2d Sess., Appendix 37 (1914).

4. 15 USC §§41-45, 52-58 (Federal Trade Commission Act of 1914 as amended by Act of Mar. 21, 1938, ch. 49, §3, 52 Stat. 111)

5. 15 USC §§12-21 (Clayton Act of 1914 as amended by Act of Dec. 27, 1950, ch. 1184, 64 Stat. 1125).

5A. 15 USC §§13, 13a (Robinson-Patman Act of 1936).

6. 15 USC 41, 44, 45, 52-58 (Wheeler-Lea Amendment to FTC Act, Act of Mar. 21, 1938, ch. 49, §3, 52 Stat. 111).

7. S. Rept. 1326, 62d Cong., 3d Sess., p. 3-4 (1913); H. Doc. 625, 63rd Cong., 2d Sess. p. 1-7 (1914); H. Rept. 533, 63rd Cong., 2d Sess., p. 2 (1914).

8. E.g. Great Atlantic & Pacific Tea Co. v. F.T.C., 106 F.2d 667 (1939); F.T.C. v. Henry Broch & Co., 363 U.S. 166, 168 (1960); F.T.C. v. Fred Meyer, Inc., 390 U.S. 341, 349 (1968).

9. Kunreuther, H., "Why the Poor Pay More For Food: Theoretical and Empirical Evidence," The Journal of Business. 46 (July 1973) No. 3: pp. 368-383.

10. 692 Antitrust & Trade Reg. Rep. (BNA) A-10, E1-13 (Dec. 10, 1974).

11. National Petroleum Refiners Assoc. v. F.T.C., 482 F.2d 672 (D.C. Cir. 1973) rev'g 340 F. Supp. 1343 (D.D.C. 197) cert. denied 94 S.C.T. 1475 (1974).

12. Pub. L. 93-637, §205 (approved Jan. 4, 1975); S.356, 93rd Cong., 2d Sess., §205 (1974).

13. In re Kellogg, F.T.C. Dkt. #8883; complaint issued 3 Trade Reg. Rep. ¶19898 as 21915-21917 (Apr. 26, 1972).

14. In re Exxon, F.T.C. Dkt. #8934; issuance of complaint announced 3 Trade Reg. Rep. ¶20388 at 20269-20271 (July 17, 1973).

15. Newsweek, June 14, 1976, p. 79

16. U.S. Bureau of Census, Annual Survey of Manufacturers (1970) Table 4, Concentration Ratio Section; also see H.R. 9182, 94th Cong., 2d Sess., Report No. 94-1338.

17. Wilson, R.E., "The FTC's Deconcentration Case Against the Breakfast Cereal Industry: A New 'Ballgame' in Antitrust?" Antitrust Law & Economics Review, Vol. 4, p. 57 (Summer 1971).

18. In re Kellogg, F.T.C. Dkt. #8883; Quaker Trial Exhibit RQ-1, Trial Transcript, at 5767-5774 (June 3, 1976).

19. In re Kellogg, F.T.C. Dkt. #8883; Quaker Trial Exhibit RQ-2, Trial Transcript, at 5774-5796 (June 3, 1976).

20. In re Kellogg, F.T.C. Dkt. #8883; Quaker Trial Exhibits RQ-1, RQ-2, Trial Transcript, at 5767-5774 (June 3, 1976).

21. In re Kellogg, F.T.C. Dkt. #8883; Quaker Trial Exhibit RQ-2, Trial Transcript, at 5774-5796 (June 3, 1976).

22. Brief for Plaintiff at Vol. II, pp. 134-135, In re Kellogg, Dkt. #8883.

23. Brief for Plaintiff at Vol. I, ¶111.13, p. 106, In re Kellogg, Dkt. #8883.

24. Plaintiff's Opening Statement, Record at p. 2803 and Brief for Plaintiff at Vol. II, p. 135, In re Kellogg, Dkt. #8883.

25. Complaint at ¶6C, In re Kellogg, Dkt. #8883, 3 Trade Reg. Rep. ¶19898 at 21916 (Apr. 26, 1972).

26. Brief for Plaintiff at Vol. II, pp. 122-134, In re Kellogg, Dkt. #8883.

27. E.g. S. Rept. 1326, 62d Cong., 3d Sess., p. 3-4 (1913) (also materials cited in Footnotes 28, 29, 30 and 32 provide further sources of such commentary).

28. Backman, Jules, "Reins on the Trustbusters," Michigan Business Papers. No. 56, pp. 15-17 (1970).

29. Bain, Joe, Industrial Organization. New York: John Wiley & Sons, Inc., 1968.