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Trade Regulations: Product Extension Merger

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RECENT DECISIONS

Trade Regulations: Product Extension Merger: In *Federal Trade Comm'n v. Procter & Gamble Co.*,[1] the Supreme Court held that the Procter & Gamble Company must divest itself of the assets of Clorox Chemical Company because, as the Commission charged, Procter's acquisition of Clorox may substantially lessen competition or tend to create a monopoly in the production and sale of household liquid bleaches. This is a violation of section 7 of the Clayton Act.[2]

Clorox was the leading manufacturer of household liquid bleach. Bleach is a distinctive product used as a germicide, disinfectant and whitening agent in washing clothes and other fabrics. There is no close substitute. The relevant bleach market is the nation and a series of regional markets, and most manufacturers are limited to competition within a single region because of high shipping costs and low sales prices. Clorox is the only firm selling nationally, and its closest competitor, Purex, has its bleach available in less than 50% of the national market. At the time of the acquisition by Procter & Gamble, Clorox had 48.8% of national sales, while Purex accounted for 15.7% of the national sales.[3]

Procter & Gamble is a large, diversified manufacturer of low price, high-turnover household products, primarily in the area of soaps and detergents, and was not a producer of household liquid bleach. Prior to its acquisition of Clorox, Procter was expanding into product lines related to its basic detergents, and was considering bleach as a possibility because of its value in washing clothes and fabrics. Procter's promotion department, however, recommended that Procter purchase Clorox rather than enter independently. Procter did acquire the assets of Clorox in exchange for Procter & Gamble stock. The Federal Trade Commission ordered divestiture but the Sixth Circuit Court of Appeals reversed the Commission.[4] The Supreme Court, subsequently reversed the Court of Appeals.

The only issue was whether the merger may substantially lessen competition or tend to create a monopoly so as to be a violation of section 7 of the Clayton Act. To find a violation of section 7, the Court must decide whether section 7 covers this type of merger, and whether section

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[1] 386 U.S. 568 (1967).

[2] 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 tend to create a monopoly, Clayton Act § 7, 38 STAT. 731, as amended, 64 STAT. 1125 (1950), 15 U.S.C. § 18.

[3] 386 U.S. 568, 571 (1967).

[4] 358 F.2d 74 (6th Cir. 1966).

7 can be used at the merger's incipiency or after the merger is a reality. The Supreme Court said that section 7 reaches all mergers whether they are vertical, horizontal, or conglomerate mergers.[5] The Court finds authority for this statement in the case of *Brown Shoe Company v. United States.*[6]

> (Congress) hoped to make plain that section 7 applied not only to mergers between actual competitors, but also to vertical and conglomerate mergers whose effect may tend to lessen competition in any line of commerce in any section of the country.[7]

Now that the Court decided that section 7 covers all mergers, it was easy to apply it to the merger in this case. The court labelled the Clorox-Procter & Gamble merger as a "product-extension" merger when it said:

> . . . this merger is neither horizontal, vertical, nor conglomerate. Since the products of the acquired company are complementary to those of the acquiring company and may be produced with similar facilities, marketed through the same channels and in the same manner, and advertised by the same media, the Commission aptly called this acquisition a 'product-extension merger.'[8]

Once the court has decided that *all* mergers come under section 7, it must then decide whether the section can be used before the merger is effective or after some post-merger evidence is introduced. The legislative history of section 7 convinced the court that "the intent . . . is to cope with monopolistic tendencies in their incipiency and well before they have attained such effects as would justify a Sherman Act proceeding."[9] In the *Brown Shoe Co. case,* the Court said:

> Congress saw the process of concentration in American business as a dynamic force; it sought to assure the Federal Trade Commission and the courts the power to brake this force at its outset and before it gathered momentum.[10]

The clear intent of Congress is to stop the anti-competitive practices before they get started so that an actual finding of anticompetitive practices is not necessary. Instead, to find a section 7 violation, the court must deal in probabilities and not certainties and must predict "the merger's impact on competition, present and future,"[11] without looking at any post merger evidence.

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[5] In United States v. General Dynamics Corp., 258 F. Supp. 36, 56, (S.D. N.Y. 1966), the court defines a conglomerate merger as one in which the merged firms are neither competitors nor potential or actual customers or suppliers of each other. The merger of competitors constitutes a horizontal merger, while the union of a firm with a customer or supplier is termed a vertical merger.

[6] 370 U.S. 294 (1961).

[7] *Id.* at 317.

[8] 386 U.S. 568, 577 (1967).

[9] S. Rep. No. 1775, 81st Cong., 2d Sess. 4-5 (1950).

[10] Brown Shoe Company v. United States, 370 U.S. 294, 317-318 (1961).

[11] 386 U.S. 568, 577 (1967).

In order to predict any anticompetitive tendencies of the merger, the court must understand the relevant market and whether or not the merger's effect "will substantially lessen competition within the area of effective competition."[12]

The Court found a violation of section 7 of the Clayton Act. "The substitution of the powerful acquiring firm for the smaller, but already dominant firm may substantially reduce the competitive structure of the industry by raising entry barriers and by dissuading the smaller firms from aggressively competing."[13] The Court continued by saying that the liquid bleach industry was oligopolistic before the merger and Procter's presence would certainly enhance pricing power to make the oligopoly more rigid.[14] Procter was a leader in products complementary to liquid bleach, and its advantages in management, advertising and manufacturing gave it a position in the liquid bleach industry greater than that of Clorox. New entrants and even existing competitors will think twice before competing with Procter & Gamble.

If the court allowed the merger to stand, it would allow the nation's largest advertiser in 1957,[15] to control a product that depends solely on advertising as its most competitive weapon. This would tend to create a monopoly if this power were fully used by Procter in selling liquid bleach.

The court also found that the merger eliminated Procter as a potential competitor in the liquid bleach industry. It's product lines were closely related to the bleach industry, and the evidence "clearly shows that Procter was the most likely entrant."[16] Procter was in the process of expanding and diversifying, and liquid bleach was certainly a possibility at the time of the merger.

The Court has done two significant things in this case. In a section 7 violation, *no* postmerger evidence will be used to prove or disprove the anticompetitive effects of the merger, and secondly, they have adopted the same test for all mergers, regardless of name.

The evidence showed that the other producers were selling more bleach for more money and "that there had been no significant change in Clorex's market share in the four years subsequent to the merger."[17] The Court of Appeals weighed this evidence quite heavily in dismissing the complaint, but the Supreme Court reversed it by merely saying that the standards were misapprehended in a section 7 proceeding.

Why was the merger struck down? The incipiency theory of section

[12] United States v. E. I. duPont de Nemours & Co., 353 U.S. 586, 591 (1957).
[13] 386 U.S. 586, 578 (1967).
[14] *Ibid.*
[15] Procter spent $80,000,000 on advertising and $47,000,000 on sales promotion in 1957. Federal Trade Commission v. Procter & Gamble Co., 386 U.S. 568 (1967).
[16] 386 U.S. 568, 576 (1967).
[17] 358 F.2d 74, 80 (6th Cir. 1966).

7 is the answer. The main purpose of the section 7 is to stop this growth towards bigness in its incipiency and to foster competition. Congress does not want to "wait and see" what the effects of the merger may be before they find a violation of section 7, Clayton Act. If they were to allow mergers of this kind, and not find a violation until the merger showed the anticompetitive effects or until the company did use its power to stifle competition, the entire purpose of the Act would be frustrated.

Thus, the Court has failed to distinguish between the various types of mergers when applying section 7. It may be a bit inflexible to use one test for all mergers, but it appears to be the best approach because the aim of section 7 is to stop anticompetitive effects—the end results of many mergers. In other words, if the proposed merger will substantially lessen competition or tend to create a monopoly, it should be stopped regardless of the name accorded to it.

MICHAEL J. O'MELIA

Products Liability: Adoption of Section 402A of the Restatement of Torts (Second) in Wisconsin.

> For products-liability cases we adopt the rule of strict liability in tort as set forth in sec. 402A of Restatement, 2 Torts(2d),[1] pp. 347, 348.[2]

The Wisconsin Supreme Court, in *Dippel v. Sciano*,[3] used these words in adopting the rule of strict liability in product liability cases. However, it is questionable if the doctrine of "strict liability," as that term is used in the *Restatement*[4] and elsewhere, was in fact adopted.

The plaintiff in *Dippel* sought to recover damages for personal injuries sustained when the front leg assembly of a large coin-operated pool table collapsed, traumatically amputating two of his toes. Plaintiff and two other men, allegedly at the request of and with the consent of the defendant tavern owner, were moving the pool table to a position

[1] Sec. 402 A. Special Liability of Seller of Product for Physical Harm to User or Consumer
(1) One who sells any product in a defective condition unreasonably dangerous to the user or consumer or to his property is subject to liability for physical harm thereby caused to the ultimate user or consumer, or to his property, if
(a) the seller is engaged in the business of selling such a product, and
(b) it is expected to and does reach the user or consumer without substantial change in the condition in which it is sold.
(2) The rule stated in subsection (1) applies although
(a) the seller has exercised all possible care in the preparation and sale of his product, and
(b) the user or consumer has not bought the product from or entered into any contractual relation with the seller.

[2] 37 Wis.2d 443, 459, 155 N.W.2d 55, 63; See also, Monograph, *Brief Opposing Strict Liability In Tort,* DEFENSE RESEARCH INSTITUTE (1966).

[3] 37 Wis.2d 443, 155 N.W.2d 55 (1967).

[4] RESTATEMENT (SECOND), TORTS §402A (1965).