Washington University Law Review

Volume 1963
Issue 2 *Symposium: The Meaning and Impact of Brown Shoe Co. v. United States*

1963

Brown Shoe: The Guidance of a Footnote

William F. Rogers

Sanford M. Litvack

BROWN SHOE: THE GUIDANCE OF A FOOTNOTE

WILLIAM F. ROGERS* AND SANFORD M. LITVACK*

Mr. Chief Justice Warren's opinion in *Brown Shoe Co. v. United States*,[1] clearly indicates that Section 7 of the Clayton Act (as amended in 1950) is the most economically significant antitrust statute ever to be written into law.

The *Brown Shoe* decision clarifies two important areas previously undefined. First, for the purpose of measuring the probable horizontal effects of a merger of two competing retailers, a city, including its immediate contiguous surrounding area, exceeding 10,000 in population was held to be a "section of the country" within the meaning of section 7. Second, and of equal significance, was the Court's proscriptions against vertical acquisitions if the acquired company occupies the position of a potential customer of the acquiring company, particularly when, as in *Brown*, this is coupled with (1) a history of no previous sales to the acquired company in the product market or submarket involved and (2) an evidenced intention to conduct such sales.

However, for future guidance in section 7 cases perhaps the most significant aspect of the decision is suggested by footnote 65 and the language of the opinion immediately preceding the footnote. Mr. Chief Justice Warren in describing the criteria to be used in determining the appropriate relevant geographic market observed:

> The fact that two merging firms have competed directly on the horizontal level in but a fraction of the geographic markets in which either has operated, does not, in itself, place their merger outside the scope of § 7. That section speaks of "any . . . section of the country," and if anti-competitive effects of a merger are probable in "any" significant market, the merger—at least to that extent—is proscribed.[65] [2]

Footnote 65 reads:

> To illustrate: If two retailers, one operating primarily in the eastern half of the Nation, and the other operating largely in the West, competed in but two mid-Western cities, the fact that the latter outlets represented but a small share of each company's business would not immunize the merger in those markets in which competition might be adversely affected. On the other hand, the fact would, of course, be properly considered in determining the equitable relief to be decreed. *Cf. United States v. Jerrold Electronics Corp.*, 180 F. Supp. 545 (D.C.E.D. Pa.), *aff'd*, 365 U.S. 567.[3]

---

* Associated with Donovan, Leisure, Newton & Irvine.

1. 370 U.S. 294 (1962).
2. *Id.* at 337.
3. *Ibid.*

Careful consideration of this footnote can provide the practicing attorney with a means for rendering more precise advice to his clients. Thus, the footnote suggests that after carefully analyzing the facts and circumstances of a particular proposed merger, the attorney should consider the possibility of partial divestiture. For even though the proposed acquisition might, on its face, have either vertical or horizontal effects which would be proscribed by section 7, these effects might be removed by severance, limited divestiture or partial acquisition.

Divestiture is, in itself, drastic relief in an antitrust suit. This is not to say, of course, that such relief has not been decreed in a number of antitrust cases. But, in view of the serious economic consequences which may flow from divestiture, the courts properly are reluctant to enter such a decree unless the government has shown absolute necessity. Accordingly, courts have sometimes attempted to limit divestiture only to that portion of the assets which is absolutely necessary to a restoration of competitive conditions. Thus, the Supreme Court, even in Sherman Act cases, has required the district courts to ascertain which properties were lawfully acquired and which unlawfully.[4]

While there have not yet been any court decisions involving limited divestiture in actions brought under amended section 7, the rationale applied to divestiture in Sherman Act cases would apply with even greater force to merger actions. Footnote 65 should afford the springboard for such applications in the future.

The government's purpose in instituting a civil antitrust action is not to penalize but rather to remedy. In section 7 cases particularly the goal is restoration of competitive conditions not punishment. Thus, as has been the rule in equity actions for centuries, the relief decreed should not exceed the injury claimed.[5]

The concept of limited divestiture is particularly applicable when the Government challenges a specific acquisition and, in addition, itemizes, as part of its complaint, a series of acquisitions dating back several years. Parenthetically it should be noted that this seems to have become a popular practice in Antitrust Division complaints.[6]

When the Government claims that the specific acquisition under attack "pushed" the company into a position in which, when the prior merger history is also considered, there may be a substantial lessening of competition or tendency to monopoly, obviously, if divestiture is necessary at all, the relief need be directed only to the most

4. See, *e.g.*, Schine Chain Theatres, Inc. v. United States, 334 U.S. 110 (1948).

5. Peck v. Goodberlett, 109 N.Y. 180, 16 N.E. 350 (1888).

6. United States v. Chicago Title & Trust Co., Civil No. 14130-3, W.D. Mo., Nov. 9, 1962; United States v. Philadelphia Nat'l Bank, 201 F. Supp. 348 (E.D. Pa. 1962).

recent acquisition. Indeed in *United States v. Jerrold Electronics Corp.,*[7] the court found that although "the cumulative effect of the entire series of said acquisitions [was] to foreclose competitors . . . ." and that "the effect of any future acquisitions may be to substantially lessen competition and to tend to create a monopoly . . . .,"[8] nevertheless the appropriate remedy was not divestiture at all but rather an injunction prohibiting future acquisitions except under certain circumstances.

Moreover, even in cases when divestiture is deemed necessary, the divestiture should be limited to the particular acquisition which violates section 7.

Likewise, if the Government claims that a series of acquisitions violate section 7, the relief to be accorded should relate only to those acquisitions which have resulted in the company's exceeding the boundaries of section 7.

The Federal Trade Commission has recently begun to recognize this basic rule of logic. In the *Foremost Dairies*[9] case, in which the commission counsel had attacked some 52 acquisitions, the Commission stated:

> We have previously rejected the argument under Section 7 that certain acquisitions in a series of acquisitions, none of which can be shown to have the adverse effect on competition required by Section 7, became illegal and may be ordered divested for the reason that the cumulative effect on competition of these prior mergers may be such as to make any future acquisition illegal.[10]

The Commission, in ordering the divestiture of only ten of the acquired companies, went on to say:

> We note, however, that an order requiring respondent to divest itself of certain corporations will to that extent dissipate the cumulative effect on competition of all these acquisitions. We have found that ten of respondent's corporate acquisitions are illegal and our order will require divestiture of these concerns.[11]

This approach might also apply with equal force when the acquired company consists of several facilities some of which are susceptible of being divested and maintained as separate effective economic units. Under this method the acquiring company might be permitted to retain that portion of the assets which would not, by itself,

7. 187 F. Supp. 545 (E.D. Pa. 1960), *aff'd per curiam,* 365 U.S. 567 (1961).

8. *Id.* at 572.

9. Foremost Dairies, Inc., TRADE REG. REP. ¶ 15877 (No. 6495, FTC, 1962).

10. *Id.* ¶ 15877, at 20690.

11. *Id.* ¶ 15877, at 20691. *Accord,* Luria Bros. & Co., TRADE REG. REP. ¶ 16299 (No. 6156, FTC, 1963); Union Carbide Corp., TRADE REG. REP. ¶ 15503 (No. 6826, FTC, 1961); Farm Journal, Inc., 53 F.T.C. 26 (1956).

violate section 7. However, in this regard it should be noted that the Supreme Court's language in *Brown*, observing that

> . . . [i]f the District Court's characterization of the relevant market is proper, the number of markets in which both Brown and Kinney have outlets is sufficiently numerous so that the validity of the entire merger is properly judged by testing its effects in those markets.[12]

indicates that when the facilities involved are sufficiently numerous the merger may be judged as a whole and the relief directed accordingly.

Although the concept of limited divestiture has not yet been applied by the courts in actions brought under amended section 7, the concept has been recognized by the Department of Justice and the Federal Trade Commission in numerous consent decrees.

According to statistics to be published by the Antitrust Section of the American Bar Association, out of the 13 cases filed under amended section 7 which were settled by the Department of Justice by consent decrees and required any form of divestiture, in only 3 has the Department received complete divestiture of the acquired assets or stock; in the balance only partial divestiture was required. The figures are equally striking in FTC cases in which the acquiring company was compelled to divest completely in only 3 out of 14 cases settled by consent.

While it is fair to assume that the government agencies are willing to settle for less in a consent decree than they would demand after trial, nevertheless a great deal may be gleaned from an examination of some such decrees.

In the *Ryder* case[13] the government attacked the acquisition by Ryder of the stock or assets of 30 companies which included more than 8,500 vehicles lease contracts, garages and other facilities. The consent decree terminating the action provided that Ryder divest itself of a total of 400 motor trucks (including lease contracts pertaining to said trucks) in 5 specified cities.[14] Thus, the defendant was permitted to retain the balance of the stock and assets attacked by the complaint. Manifestly the government recognized that effective competition could be restored without total divestiture.

---

12. Brown Shoe Co. v. United States, 370 U.S. 294, 338 (1962).

13. United States v. Ryder System, Inc., 1961 Trade Cas. ¶ 70056 (S.D. Fla. 1961).

14. The district court subsequently modified the judgment to decrease the number from 400 to 360 and increase the time to sell. United States v. Ryder System, Inc., 1962 Trade Cas. ¶ 70443 (S.D. Fla. 1962).

In similar fashion the decree in the *Hilton Hotels* case[15] provided for the divestiture of only 3 hotels in 3 separate cities. The complaint had originally demanded divestiture of approximately 34 hotels in 4 different cities. Thus here, too, the government was willing to limit its demands and accept partial divestiture sufficient to accomplish the aims of the lawsuit.

Although there are many other Department of Justice and FTC cases which, like *Ryder* and *Hilton,* did not require complete divestiture, a review of every one is unnecessary.[16]

Suffice it to note that the pattern has been, and the trend continues to be, that the government will consider and accept settlement of section 7 cases on a partial divestiture basis. This approach in consent decrees might well be carried over, with profit, by the government to litigated decrees. The courts would likely welcome a refreshing approach whereby the government limited its divestiture demands to those believed absolutely necessary. Otherwise, a court might wonder why the government can accept limited divestiture in a consent decree but demand total divestiture after trial. The public interest and public need is the same whether the case is disposed of by consent or trial since all the government should require is an alleviation of the harmful effects; the relief should be limited to effectuate only that goal.

While footnote 65 suggests the type of relief to be afforded once suit has been instituted, it also suggests the possibility of severance at or about the time of the proposed acquisition. This could avoid the commencement of any action or, at least, preclude a finding of illegality. The severing knife must be skillfully applied to particular aspects of the business of either the acquired or acquiring corporation in order to remove the anti-competitive effects. Thus a prohibited acquisition would be converted into a permissible one. Perhaps the most facile means for effectuating the desired result would be to place the assets sought to be severed into a separate division of the corporation. Having done this the problem of the most appropriate method of severing the division from the corporation comes to the fore.

Severance of the division from the corporation will, of course, raise a number of corporate problems concerning the form of the severance,

---

15. United States v. Hilton Hotels Corp., 1956 Trade Cas. ¶ 68253 (N.D. Ill. 1956).

16. See, *e.g.*, United States v. Suburban Gas, 1962 Trade Cas. ¶70439 (S.D. Cal. 1962); United States v. National Homes Corp., 1962 Trade Cas. ¶ 70533 (N.D. Ind. 1962); United States v. Hertz Corp., 1960 Trade Cas. ¶ 69762 (S.D.N.Y. 1960); United States v. American Radiator & Standard Sanitary Corp., 1960 Trade Cas. ¶ 69810 (W.D. Pa. 1960); United States v. Minute Maid Corp., 1955 Trade Cas. ¶ 68131 (S.D. Fla. 1955); Continental Baking Co., FTC Dkt. No. 7880 (1962); Minnesota Mining and Mfg. Co., FTC Dkt. No. 7973 (1961); Diamond Crystal Salt Co., FTC Dkt. No. 7323 (1960).

the timing involved, the nature of the consideration received and the requirements of the Securities Act of 1933.[17] While severance of the division from the corporation may be accomplished by many means, consideration of the following methods will suffice to exemplify some essential problems:

(1) New subsidiary formed by the corporation and assets of the division transferred to it, and the securities of the new subsidiary distributed to shareholders of the corporation.

(2) New subsidiary formed as in (1), but the securities thereof sold for cash, other securities or assets or a combination thereof.

(3) Sales of assets of the division.

Alternative (1) lacks appeal, since it will constitute a partial liquidation of the corporation and therefore is not apt to be attractive to the management of the corporation.[18] Further, if the securities of the corporation are closely held, this method may not solve the antitrust problems.

Turning to the more complicated alternatives (2) and (3), it is clear that a sale for cash of the securities of a subsidiary consisting of the division, or a sale for cash of the division's assets presents no unusual corporate problems. Negotiations will, of course, arise as to representations and warranties made by the corporate seller.

The acquisition of assets in exchange for the stock or assets of the division or an exchange of assets for the division's assets, is substantially more complicated. Thus, the nature and description of the assets being acquired or disposed of, liens thereon and title thereto, payment of current real estate taxes, assignment of patents, trade marks, trade names and like matters incident to a sale or purchase of assets constituting a part of a going concern, are complicated, but no more so than the usual sale or acquisition of assets.

In the event all, or substantially all, (and in some cases, a substantial part or an integral part) of the assets of a corporation are to be sold incident to the severance of the division or the acquisition of assets in exchange therefor, the applicable state statutes must be reviewed; many states require an approving vote of stockholders for such a sale.[19] If the selling corporation's stock is "listed" on a National Securities Exchange, a proxy statement will be necessary to solicit proxies, in compliance with section 14 of the Securities Act of

17. 48 Stat. 74, 15 U.S.C. §§ 77(a)-(aa) (1958).

18. Alternative (1), in addition to simplicity, has the advantage of not requiring compliance with the Securities Act of 1933 since a dividend is not deemed a "sale" under § 2(3) of that act because the transaction is not deemed an offer or sale "for value." 1 LOSS, SECURITIES REGULATION 517-18 (2d ed. 1961).

19. In New York a two-thirds favorable vote is required with right of appraisal to dissenters. N.Y. STOCK CORPORATION LAW § 20.

1934.[20] Thus the rules of the applicable stock exchange must also be reviewed.

Even when, as noted, the method for severance has been determined, the parties must still consider the timing of the severance and the consideration to be furnished.

The timing of the disposition of the division will call for careful consideration and probably consultation with the purchaser. It would, of course, be less complicated if the severance of the division could be accomplished prior to the date of its sale. However, since the consideration received upon the sale is related to the demands and wishes of the purchaser, in most cases it will be feasible to make only a tentative severance of the division prior to its actual sale. Therefore, the actual sale of the division will, in all probability, take place at or about the same time as the proposed merger.

In addition, apart from the usual wish of the purchaser to acquire assets (in order to permit future depreciation charges thereon), the form of the consideration to be received for the division, if other than cash, will be an important factor affecting the antitrust aspects of the contemplated severance. Thus, if securities represent the entire consideration or a substantial part thereof, attention must be given to the type of securities to be delivered. Clearly, debt securities will raise fewer problems since they will not carry with them any voting rights, and, preferably, will not be secured by any mortgage on the assets sold or a pledge of any voting securities. If corporate stock is delivered as consideration for the sale of the division the problem of affiliation of the purchaser and the seller will arise. The transfer of a substantial amount of the voting stock of the purchaser may vitiate the over-all object sought to be accomplished by the sale of the division. The corporation would then have substantial voting power and the antitrust problems might still be present.

The effect of the Securities Act of 1933 should be remembered throughout the negotiations. Where securities are received as part of the consideration for the sale of the division, the corporation may or may not wish to retain these securities as part of its assets. If the corporation contemplates a resale of these securities, the Securities Act of 1933 will be applicable and registration under that act will be required unless the securities are privately placed with a very limited number of purchasers from the corporation who clearly are taking for investment. In the event these subsequent purchasers make a public distribution of the securities purchased, the corporation will be an "underwriter" under the Act of 1933 and have the liabilities attrib-

20. 48 Stat. 895, 15 U.S.C. § 78(n) (1958).

uted thereto,[21] including the danger of participating in a criminal violation[22] of the act, namely, the public distribution of securities without exemption or registration under that act. Therefore, if securities are taken by the corporation, it should, if possible, persuade the issuer to register these securities under the Securities Act of 1933.

Prior to making even a tentative severance of the division, consideration must, of course, be given to the tax consequences. The tax consequences to the selling corporation and to the purchaser may force the form of severance to follow prescribed and artificial maneuvers.

CONCLUSION

The decision in *Brown Shoe* is a landmark in the antitrust field. The case will undoubtedly be cited and recited, applied and misapplied, distinguished and compared but certainly not ignored. Perhaps, as some have suggested, the opinion leaves more questions unanswered than answered. Nevertheless it may well be that in the long run the implications of footnote 65 will have the most significant impact on future antitrust litigation. The words of the Court can act as a guide to the practicing attorney in advising clients in the future. The Court has suggested a means whereby the skillful attorney may either be able to transform an otherwise illegal merger into one which would not violate section 7 and avoid suit or, once suit has been commenced, effectuate a settlement which will not require total and complete divestiture. Thus the terms "severance, limited divestiture, and partial acquisition" may well become basic ingredients of every attorney's vocabulary when considering a proposed merger.

---

21. Failure to register [48 Stat. 78, 15 U.S.C. § 77(f) (1958)] imposes civil liabilities [68 Stat. 686 (1954), 15 U.S.C. § 77(*l*) (1958)] on the "seller" of the securities, with right of rescission by the purchaser for a three year period [48 Stat. 908 (1934), 15 U.S.C. § 77(m) (1958)].

22. Penalties—48 Stat. 87, 15 U.S.C. § 77(x) (1958).