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United States v. E. I. DuPont de Nemours and Company

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Case Comment

UNITED STATES v. E. I. DUPONT DE NEMOURS AND COMPANY — The famous DuPont case was in the courts for ten years. This comment is primarily an analysis of a few interesting points made by LaBuy J., of the Seventh Circuit, in an opinion dated November, 1959,[1] on reference for settlement from the Supreme Court as a result of its finding on June 3, 1957,[2] that the DuPont Company had violated the Anti-Trust Law. It is therefore necessary to review the Supreme Court's findings briefly to understand LaBuy J.'s judgment. Much of the argument in this protracted litigation is relevant to Canadian problems, and the cardinal emphasis will be placed upon matters of interest to Canadian readers.

Although DuPont had been charged under several provisions of the American Anti-Trust laws, the Supreme Court found it guilty only of a violation of section 7 of the Clayton Act. The relevant part of that section provided:[3]

> That no corporation engaged in commerce shall acquire, directly or indirectly, the whole or any part of the stock or share capital of another corporation engaged also in commerce, where the effect of such acquisition may be to substantially lessen competition between the corporation whose stock is so acquired and the corporation making the acquisition, or to restrain such commerce in any section or community, or tend to create a monopoly of any line of commerce.

A majority of the Supreme Court, in an opinion written by Brennan J.,[4] held that, although General Motors and DuPont were not competitors, nevertheless a violation of the Act had occurred. This reversed the exhaustive opinion of LaBuy J., which ran to 100 pages in a close analysis of the forty-year relationship between these two industrial giants.[5] The violation resulted from DuPont's purchase, in the years from 1917 to 1919, of General Motors' stock which at the date of trial totalled 63,000,000 shares, representing a 23% interest in the company.[6] The objects of this purchase, as shown by voluminous evidence, were two-fold. First, the directors of DuPont felt that an investment in the automobile industry would be a profitable long-term employment of capital. Second, it was felt that such a purchase would protect DuPont against a loss of its position as commanding supplier in the field of enamels and other chemical products used by the automobile industry. There was genuine reason to fear that the success of the Ford Motor Company might lead to Ford's investment in supplier companies, thus eventu-

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1 177 F. Supp. 1.
2 353 U.S. 586, 77 S. Ct. 872.
3 Amended in 1950. Not material.
4 77 S. Ct. 872 at p. 877.
5 126 F. Supp. 235.
6 This original purchase by DuPont is closely analogous to the investment made last autumn by Canada Cement Ltd. in shares of Standard Paving and Materials Ltd.

ally freezing out independent chemical producers. Indeed, the success of Ford very nearly resulted in bankruptcy for General Motors in the early twenties. Faced with a threatened loss of this substantial investment, DuPont loaned some of its managerial talent and capital to the floundering company. The result of such infusion was that, although more than one hundred automobile producers were defunct by 1932, General Motors survived.

With this background it is possible to examine the majority opinion in the DuPont case. One fascinating feature of the opinion is that DuPont was convicted in 1957 for a purchase made 40 years earlier that had not infringed the public interest but might do so in the future. The following excerpts from the opinion of Brennan J. are noteworthy:[7]

> We agree with the trial court that considerations of price, quality and service were not overlooked by DuPont or General Motors. Pride in its products and its high financial stake in General Motors' success would naturally lead DuPont to try to supply the best. . . .
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> . . . We repeat that, the test of a violation of s. 7 is whether, *at the time of suit*, there is a reasonable probability that the acquisition is likely to result in the condemned restraints. . . . The fire that was kindled in 1917 continues to smolder. It burned briskly to forge the ties that bind the General Motors market to DuPont, and if it has quieted down, it remains hot, and . . . is likely at any time to blaze and make the fusion complete. (Italics are mine.)

The celestial fire that impregnates the last sentence would be excellent embellishment for a tract against big business, but seems out of place in a court of law.

Another question arises in reference to the Court's holding that the test must be applied "at the time of suit". The dissenting view was that the Government must show DuPont's purchases tended to create a monopoly at the date of the purchase. In view of the weakness of General Motors at the time, this would be impossible. Furthermore, this interpretation would rule out that part of the Government's case which was based on the fact that the subsequent broad diffusion of General Motors stock among thousands of small shareholders gave DuPont's 23% interest effective control.

The wisdom of this viewpoint is apparent, from a utilitarian aspect, when one considers the ramifications of the Supreme Court's opinion in the DuPont case. It means that an external authority can apply a new set of motives at any time in the future to invalidate a formerly lawful act.

Although the Clayton Act was enacted in 1914, this is the first case in which it was applied to a vertical acquisition.[8] Furthermore, it is the first time it was used against an investment that had taken

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[7] 77 S. Ct. 872 at p. 884.

[8] A key point to note is the difference between horizontal and vertical mergers. Generally speaking, a horizontal merger results when a company acquires control of another company competing in the same market; a vertical merger (or integration) results when a supplying company acquires control of a corporate customer of its products.

place years before. In regard to these two points, the vigorous dissenting opinion of Burton and Frankfurter JJ. is instructive:[9]

> The Court, in accepting both of these contentions, disregards the language and purpose of the Statute, 40 years of administrative practice, and all the precedents except one District Court decision. The sweeping character of the Court's pronouncement is further evidenced from the fact that to make its case the Court requires no showing of any misuse of a stock interest either at the time of acquisition or subsequently to gain preferential treatment from the acquired corporation. All that is required, if this case be our guide, is that some court, in some future year be persuaded that a "reasonable probability" then exists that an advantage over competitors in a narrowly construed market may be obtained as a result of the stock interest.

The dissenters also point out that the majority judgment is based on the "fact" that DuPont had no standing as a General Motors supplier before 1917, and gained a commanding position afterward:[10]

> With these words the Court overturns the unequivocal findings of the District Court to the effect that DuPont was a principal supplier to General Motors prior to the 1917-1919 stock purchase, that DuPont maintained its position in the years following the stock purchases, and that for the entire 30-year period preceding the suit, General Motors' purchases of DuPont's products were based solely on the competitive merits of those products.

This is an accurate summation of LaBuy J.'s opinion[11] which analyzed in detail all purchases of DuPont products made by General Motors. He found that the various divisions of General Motors bought separately and competed with each other. Where DuPont products, like Duco enamel, were used exclusively, it was because they were superior to others, as shown by the purchases by Ford, Chrysler and other companies. The decentralization of authority at General Motors was an important point. Each division was an autonomous company, and executives from other divisions were not even allowed in to examine the models. As a result, some divisions of General Motors continued to buy products of DuPont competitors at a time when other divisions were sticking to DuPont products. Duco was used by Cadillac for three years before other divisions began to buy it, and this was after Ford had begun to use it on all its products.

In spite of such hard economic facts, DuPont was convicted.[12] The Supreme Court referred the matter to the District Court to effect a settlement of the complex problems posed by its findings.

LaBuy J.'s decision on the reference is another lengthy, reasoned look at the economics of the case. The Government urged that DuPont be ordered to divest itself of its 63,000,000 shares, which were worth $3.5 billion at the date, by declaring the shares as dividends to DuPont shareholders. They would thus be taxable at the full rate, ranging up to 92%. The Court was also asked that, all General Motors shares which Delaware and Christiana Securities

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[9] *Supra,* footnote 10 at p. 885.
[10] *Supra,* footnote 10 at p. 895.
[11] *Supra,* footnote 4.
[12] *Supra,* footnote 2.

(two holding companies) would receive under this plan as large Dupont shareholders, be sold by a trustee. Since these two companies held approximately 13,500,000 shares, this would mean that more than 19,000,000 General Motors shares would be sold from their holdings alone. If these large figures are meaningless, it might be pointed out that, even on a day of active trading, General Motors shares rarely turn over a volume of 50,000 shares on the stock exchanges.

LaBuy J. points out the obviously disastrous effect that such a plan would have on the 230,000 DuPont and the 700,000 General Motors stockholders. He reviewed the testimony from dozens of shareholders in the two companies who ranged from individuals owning less than twenty shares, to a few with substantial holdings. They all testified that if the Government's demands were accepted, they would be forced to sell most of their holdings immediately. It is clear that such a plan would result in millions of shares being dumped on the market in a few weeks' time, which would probably lead to a market crash of 1929 proportions. The shareholders would thus be punished for a crime to which they were never parties. Furthermore, the two companies involved would find it very difficult to raise capital needed for growth.

It may be objected that such arguments are irrelevant. If DuPont is guilty, then the price must be exacted. "Let him look to his bond," Shylock shrieked, and the law was not to take cognizance of the indisputable fact that Antonio would die as a result. Franz Kafka depicts in his novel, *The Trial,* a system of law that exists as a paralysing miasma, obsessed with its narrow legalities, and totally oblivious of human rights. However, law can never operate in a vacuum. Decisions like *Donoghue (M'Allister) v. Stevenson*[13] are examples of a view that law must not cease to serve human needs.

With such a terrible prospect of economic chaos, the learned judge in effecting the settlement, masterfully presented a way out of the dilemma. He stated that the Government's delay had created a detrimental reliance, an equitable doctrine that sounds strangely foreign to anti-trust law:[14]

> Moreover, the Government itself cannot escape responsibility for the plight of these stockholders. At the time of acquisition, there existed a very small fraction of the present number of stockholders of the corporations involved. It waited some thirty years after the acquisition occurred before bringing this action.
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> It should, therefore, recognize that stockholders who purchased DuPont in those intervening years had every reason to believe that DuPont's holding of General Motors was entirely proper and legal.

His conclusion was that DuPont be stripped of its voting rights on its General Motors shares, but that it be allowed to retain the shares as an investment. The voting rights were to pass through to

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[13] [1932] A.C. 562.

[14] *Supra,* footnote 1 at p. 13.

DuPont shareholders, giving them full rights as General Motors shareholders at General Motors meetings. Furthermore, no DuPont representatives were to sit on the Board of General Motors.

This is an ingenious solution that should remove all taint from the investment, even where the most zealous "trustbusters" on the Supreme Court are concerned. It is amusing to reflect that Frankfurter J., who wrote such a scathing indictment of the Court in the dissent, was appointed by President Roosevelt for his liberal views, and was generally regarded by American conservatives as a fiery radical. The Warren Court has been the centre of controversy for six years because of its alleged "legislative" actions. If Justice Frankfurter's views be correct, then the Court was here overturning judicial precedent to carry out a legislative objective.

The American Constitution is built on the premises that functions are divided between the Legislative, Executive, and Judicial branches of Government. It is true that a certain overlap is necessary, but it is questionable whether an appointed Court should usurp the functions of the democratically elected legislature. If LaBuy J.'s settlement is upset by the Supreme Court in favour of the Government's plan, then the question of the Court's role will become a vitally important political question, since the resultant economic dislocation will frustrate the legislator's plans for a booming economy.

A Bill was introduced in the American Senate last year which sought to curb the Supreme Court from some of its more enthusiastic ventures. It was voted down, but the fact that a number of distinguished legislators voted for it shows how deep the mistrust of the Supreme Judicial authority is in many thoughtful quarters. This reprimand may well be instrumental in preventing the Court from overruling the learned District Court Judge. If his decision stands, it could quite conceivably be a watershed in the annals of Government regulation of business for its judicious balancing of the respective interests of the general public and the investor.

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