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THE UNITED STATES, DEVELOPING COUNTRIES AND THE ISSUE OF INTRA-ENTERPRISE AGREEMENTS*

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United Nations meetings in recent years have been characterized by an oscillation in the relationship between industrial and developing countries with regard to issues concerning transnational enterprises and international investment. At times the atmosphere has seemed clouded with recriminations, suspicion and mutual misunderstanding. For brief periods the tension has been lightened by agreement on what appear to be common goals and aspirations. However, such high points are often followed by a descent into continuing controversy.

In the antitrust field, an apex of unanimity was the resolution adopted by the Seventh Special Session stating that: "Restrictive business practices adversely affecting international trade, particularly that of developing countries, should be eliminated and effort should be made at the national and international levels with the objective of negotiating a set of equitable principles and rules."[1] Consensus on this goal provided the momentum for a more detailed resolution at the Nairobi UNCTAD (United Nations Conference on Trade and Development) calling for work by a group of experts on a four point agenda dealing with the elimination of restrictive business practices.[2]

The work of this expert group has begun and will be continued in the spring. A little progress has been made, but very substantial areas of disagreement and divergence remain. The "Northern" and

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[1] G.A. Res. 3362, 7 U.N. GAOR Supp. 1, at 4, U.N. Doc. A/10301 (1975).

[2] Omnibus Resolution, Nairobi Conference, U.N. Doc. TD/217 (May 5, 1976), § 96(4).

"Southern" nations are far apart on issues such as whether principles should be binding or voluntary, whether there should be special exemptions for cartels originating in developing countries and whether foreign enterprises may be treated differently than domestic ones. This paper, however, will deal primarily with what may appear to be a more limited and technical issue, but one that is really quite fundamental in the current U.N. scene. That issue is how a set of international antitrust principles should deal with restrictive arrangements between a foreign parent corporation and its local subsidiary, particularly where that subsidiary is in a developing country.

The question of parent-subsidiary relationships is a complex and debatable one even under well settled and relatively conservative bodies of antitrust law such as those of the United States and of the European Economic Community (EEC).

Under American law, it is relatively clear that an antitrust conspiracy may not be based upon an alleged agreement between a corporation and its officers or branches.[3] After that, clarity is scarce. On the one hand, there is a substantial body of law to the effect that the free business choice to set up two separate corporate legal entities entitles persons who deal with those entities and government regulators to treat each entity as an independent corporation and to subject transactions or agreements among such entities to the strict prohibitions contained in the antitrust laws. In major antitrust opinions from *Yellow Cab*[4] through *Kiefer-Stewart*[5] to *Perma Life*,[6] the Supreme Court has ruled that arrangements between affiliated corporations are subject to section 1 of the Sherman Act,[7] particularly if parent and subsidiary cooperate to injure competitors or hold themselves out to the public as separate competing firms. In *Perma Life* the Court stated this rule very broadly as follows: "[S]ince respondents . . . availed themselves of the privilege of doing business through separate corporations, the fact of common ownership could not save them from any of the obligations that the

[3] *See, e.g.*, Chapman v. Rudd Paint & Varnish Co., 409 F.2d 635 (9th Cir. 1969); Zelinger v. Uvalde Rock Asphalt Co., 316 F.2d 47 (10th Cir. 1963); Nelson Radio & Supply Co. v. Motorola, Inc., 200 F.2d 911 (5th Cir. 1952), *cert. denied*, 345 U.S. 925 (1953); United States v. Memphis Retail Package Stores Ass'n, 334 F. Supp. 686 (W.D. Tenn. 1971); Schoenberg Farms, Inc. v. Denver Milk Producers, Inc., 231 F. Supp. 266 (D. Colo. 1964).

[4] United States v. Yellow Cab Co., 332 U.S. 218 (1947).

[5] Keifer-Stewart Co. v. Joseph E. Seagram & Sons, Inc., 340 U.S. 211 (1951).

[6] Perma Life Mufflers v. International Parts Corp., 392 U.S. 134 (1968).

[7] 15 U.S.C. §§ 1-7 (1970).

law imposes on separate entities."[8]

However, in a number of lower court decisions, judges have refused to find illegal conspiracies based on the simple allegation that a parent and wholly-owned subsidiary agreed to fire one distributor and hire another,[9] or agreed to use the same price list.[10] Also, in the 1962 *Sunkist* case,[11] the Supreme Court dealt more leniently with the question whether antitrust liability could be premised upon a price and market allocation agreement among three interrelated but separately incorporated farmers' cooperative organizations. The Court held that there was no unlawful conspiracy. Its reasoning was that:

> To hold otherwise would be to impose grave legal consequences upon organizational distinctions that are of *de minimis* meaning and effect . . . . There is no indication that the use of separate corporations had economic significance in itself or that outsiders considered and dealt with the three entities as independent organizations.[12]

In the more recent *C & S Bank* case, the Supreme Court stated, "[t]he central message of the Sherman Act is that a business entity must find new customers and higher profits through internal expansion—that is, by competing successfully rather than by arranging treaties with its competitors."[13] While noting that "this Court has held that even commonly owned firms must compete against each other, if they hold themselves out as distinct entities,"[14] the Court pointed out "the total lack of realism in suggesting that C&S might have founded new banks that would have competed vigorously with it and with each other . . . ."[15] Relying on this reasoning, the opinion then holds that, in light of state legislation preventing C&S from expanding into new territories by direct internal growth, "C&S's program of founding new *de facto* branches, and maintaining them as such, did not infringe §1 of the Sherman Act."[16]

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[8] 392 U.S. at 141-42.

[9] Hudson Sales Corp. v. Waldrip, 211 F.2d 268 (5th Cir.), *cert. denied*, 348 U.S. 821 (1954); Alpha Distributing Co. v. Jack Daniel's Distillery, 207 F. Supp. 136, 137-38 (N.D. Cal. 1961), *aff'd*, 304 F.2d 451 (9th Cir. 1962).

[10] United States v. Arkansas Fuel Corp., 1960 Trade Cas. ¶ 69, 619 at 76,496 (N.D. Okla. 1960).

[11] Sunkist Growers, Inc. v. Winckler & Smith Citrus Prod. Co., 370 U.S. 19 (1962).

[12] *Id.* at 29.

[13] United States v. Citizens & Southern Nat'l Bank, 422 U.S. 86, 116 (1975).

[14] *Id.* at 116.

[15] *Id.* at 119.

[16] *Id.* at 120.

The enforcement policy of American antitrust agencies has consistently been to refrain from challenging arrangements between closely affiliated firms except in special circumstances, notably when affiliation eliminates actual or potential competition with a preexisting competitive firm or when agreements between affiliated firms are employed to engage in predatory practices and entrench a monopoly position.

On January 26, 1977, the Justice Department issued an *Antitrust Guide for International Operations*,[17] consisting of a set of example cases followed by analyses indicating the Antitrust Division's policy in regard to important issues of international antitrust enforcement. The first example case dealt with a major multinational corporation organized into separate national subsidiaries which referred business to each other on the basis of assigned territories. In regard to this fact situation, the *Antitrust Guide* states:

> The Department of Justice has consistently accepted the view stated in the 1955 *Report of the Attorney General's National Committee to Study the Antitrust Laws:* a parent corporation may allocate territories or set prices for the subsidiaries that it fully controls. The Department's test has generally been formulated in terms of whether the parent controls a majority of the voting stock of the subsidiary. However, the same reasoning may apply to a minority position where the U.S. firm maintains effective working control.
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> Where majority stock control is not present, the Department may make a careful inquiry into the facts of the particular case.[18]

Under Common Market law, the general rule appears to be that stated by the Court of Justice in the *Sterling Drug-Centrafarm* case, that article 85 of the Treaty of Rome[19] is not violated by

> [a]greements or concerted practices between undertakings belonging to the same group in the form of parent company and subsidiary, if the undertakings form an economic unit within which the subsidiary does not have real autonomy in determining its line of conduct on the market and if the agreements or practices

[17] U.S. DEP'T OF JUSTICE, ANTITRUST GUIDE FOR INTERNATIONAL OPERATIONS (1977).

[18] *Id.* at 12-13.

[19] Treaty Establishing the European Economic Community, *done* Mar. 25, 1957, in OFFICE FOR OFFICIAL PUBLICATIONS OF THE EUROPEAN COMMUNITIES, TREATIES ESTABLISHING THE EUROPEAN COMMUNITIES 163 (1973). Another English version, although unofficial, may be found at 298 U.N.T.S. 11.

> have the aim of establishing an internal distribution of tasks between the undertakings.[20]

On the other hand, the EEC Commission has ruled in the *Kodak*[21] case that identical conditions of sale applied on subsidiaries by the parent company could be considered as agreements between enterprises and made subject to the rules governing contracts which tend to isolate national markets or maintain price disparities between Member states.[22]

This ambivalence in Western antitrust treatment of the intracorporate arrangements is reflected in the one international declaration on this subject, which is the second of the competition guidelines promulgated by the OECD (Organization for Economic Cooperation and Development) in June 1976. That guideline states that enterprises should "allow purchasers, distributors and licensees freedom to resell, export, purchase and develop their operations consistent with law, trade conditions, the need for specialisation and sound commercial practice . . . ."[23] The guideline is silent regarding whether it applies to distributors, purchasers or licensees which are affiliated with the seller or licensor. The more natural reading is that such affiliated firms are subject to the guideline. It should be noted, however, that this provision is not worded as a traditional antitrust prohibition, but rather in the form of affirmative encouragement. It is thus arguable that Western negotiators were prepared to go somewhat beyond well settled law when they were confident that what they were writing was a voluntary guideline reflecting competition policy and trade policy rather than a rule of prohibition which might well become binding internationally or by adoption as national law. Such confidence would obviously be misplaced in the United Nations context where developing countries have emphasized their desire for a legally binding code and their wish that, at the very least, the principles and rules adopted should provide a basis for legislation in developing countries.[24]

The most striking fact about the developing country position at

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[20] Centrafarm BV v. Sterling Drug, Inc., [1974] COMM. MKT. L. R. 480.

[21] Re Kodak, [1970] COMM. MKT. L. R. *R.P. Supp.* D 19.

[22] *Id.*

[23] OECD, INTERNATIONAL INVESTMENT AND MULTI-NATIONAL ENTERPRISES 15 (1976). For background of OECD developments in antitrust and analysis of the content of the OECD text, *see* Joelson, *The Proposed International Codes of Conduct as Related to Restrictive Business Practices*, 8 LAW & POL'Y INT'L BUS. 837, 848-52, 861-69 (1976).

[24] *See generally* Roffe, *International Code of Conduct on Transfer of Technology*, 11 J. WORLD TRADE L. 186 (1977).

UNCTAD is that these nations see intracorporate restrictions not as a minor technical issue of antitrust policy but as the most important group of restrictive practices which they wish to have eliminated. This is for many reasons. These nations recognize that international cartels among private firms are much rarer than in the 1930's. Secondly, developing countries are reluctant to support broadly worded condemnations of cartels for fear of casting aspersions on their own raw material cartels. Thirdly, their own experience has been that many of the largest firms manufacturing or selling on a substantial basis in their territory are subsidiaries of multinational enterprises. Therefore, to them, how to deal with the power and practices of such subsidiaries is the central question in the restrictive practice area. Lastly, the developing countries, hungry for trade and foreign exchange earnings, take the American phrase "restraint of trade" quite literally. They would use it to justify an approach in which the acceptability of any business practice should be judged in terms of whether it restricts or restrains their export trade or the opportunity for enterprises incorporated in their country to purchase on the most favorable terms possible. They are unconvinced by the contention that restraint of trade has always meant restraint of *competition* or that "restrictive business practices" has always referred to restrictions on *competition*. This difference in approach can be summarized in another way. Delegates from nations with a long antitrust tradition have tended to argue that the international goal should be to assure that traditional restrictive business practices do not hamper international trade or the trade and development of developing countries. The developing countries have argued that any practice which has the effect of limiting their trade or development should be condemned as a restrictive business practice.

My personal view is that this issue cannot and should not be resolved solely in terms of legal precedent or conceptual analysis. As Justice Holmes taught us, the life of the law has been guided less by abstract logic than by experience and the felt necessities of the time.[25] One such necessity is the desire of developing countries that enterprises organized in their countries obey their law and further their trade interests, regardless of the subsidiary status of some of these companies. It is thus an inescapable reality that corporate subsidiaries will have to adjust their economic conduct so as to be viewed as assets to the host country, regardless of what is negotiated

[25] *See* O.W. HOLMES, JR., THE COMMON LAW 1 (1881).

in an international code for multinational enterprises. But the other crucial reality, which Western delegates will undoubtedly stress, is that foreign investment and the creation of new, potentially competitive entities are voluntary decisions which enterprises will undertake only if, in light of the perceived rules and circumstances, the benefits of such decisions outweigh the detriments and risks. Put more simply, the most relevant policy question appears to be whether multinational enterprises would be significantly deterred from creating and improving foreign subsidiaries if they were faced with rules denying them control of the buying and selling policies of such subsidiaries. A quantitative answer to such a question seems highly unlikely. Nevertheless, the consequences of a decline in international investment activity would be so serious for the world economy that both developed and developing countries must consider very carefully before imposing radically different rules of the game on multinational enterprises.

It should be noted that restrictions on competition *between* subsidiaries may well be more in the interest of host countries than of the multinational which may have agreed to such a scheme because of local demands. New foreign subsidiaries are in a sense "infant industries," development of which may require at least temporary protection against outside competition from the same product or brand.

This analysis suggests that intracorporate restrictions should be treated at the international level, not as never being a restrictive business practice or always being a restrictive business practice, but in terms of the rule-of-reason analysis developed in United States cases in regard to vertical or distribution restraints, which analysis is closely approximated by the Common Market treatment of similar practices.[26] Under such an analysis, it would be necessary to examine the market power of the multinational in the relevant markets, the degree of independence of the subsidiary, the purpose of the restraint and the relationship between the scope and duration of the restraint and any legitimate purposes for it. Moreover, even carefully qualified rules against restrictions on subsidiaries should deal only with basically commercial decisions such as sales, resales and purchases. Investment-related decisions, such as what the subsidiary should manufacture, where it should be located, and how it

[26] *See* Davidow, *Extraterritorial Application of U.S. Antitrust Law in a Changing World*, 8 LAW & POL'Y INT'L BUS. 895 (1976).

should be managed, should be dealt with outside of the international restrictive business practice context. Such an approach would not guarantee *carte blanche* for the multinational to impose and maintain all the restrictions it wishes on all types of subsidaries, but it is clear that developing countries would not tolerate such a situation in any event.

Certainly, a major reason for participating in the drafting of international principles and rules is the belief that our involvement will cause the final product to be more reasonable, more sophisticated and more pro-competitive than would be the case if the rules were written entirely by nations with little previous experience in antitrust enforcement and the fostering of a free market economy. For reasons such as this we are participating in this exercise. It may well be that in doing so, we will learn, as well as teach, more about enigmatic subjects such as intra-enterprise agreements.