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memo	~~From Aaron to The President (2 pp.) re: Certification of of Yemen Arms Sales/enclosed in Hutcheson to Brzezinski 3/7/79~~ opened per RAC NLC-126-16-28-1-3 8/6/13	3/7/79	A

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THE PRESIDENT'S SCHEDULE

Wednesday - March 7, 1979

8:15	Dr. Zbigniew Brzezinski - The Oval Office.
9:30	Mr. Frank Moore, Mr. Dan Tate, and Mr. Bill Cable - The Oval Office.
10:30	Mr. Jody Powell - The Oval Office.
11:30 (30 min.)	Vice President Walter F. Mondale, Admiral Stansfield Turner, Mr. David Aaron, and Mr. Hamilton Jordan - The Oval Office.
12:30 (60 min.)	Lunch with Vice President Walter F. Mondale, Secretary Michael Blumenthal, FRB Chairman William Miller, Mr. Charles Schultze and Mr. James McIntyre - The Cabinet Room.
2:30 (15 min.)	Attorney General Griffin Bell - The Oval Office.
5:30 (30 min.)	Meeting with Congressional Group. (Mr. Frank Moore) - The Cabinet Room.
6:10	Depart South Grounds via Helicopter en route Andrews Air Force Base and Trip to Egypt and Israel.

THE WHITE HOUSE
WASHINGTON

07 Mar 79

Stu Eizenstat

The attached was returned in the President's outbox today and is forwarded to you for appropriate handling.

Rick Hutcheson

Stu - please notify affected parties.

ID 790912

THE WHITE HOUSE

WASHINGTON

March 2, 1979

Stu - * Go over this decision memo with Brock re subtle differences re "phasing in". Where there remains a difference, let Brock decide - J

MEMORANDUM FOR: THE PRESIDENT

FROM: STU EIZENSTAT Stu
BILL JOHNSTON

SUBJECT: Rail Deregulation

As you know Secretary Adams has submitted his recommendations concerning rail deregulation. During the past month we have discussed Adams recommendations with rail management and labor, with shippers, port operators, and state and local officials, as well as with Congressional members and staffs, cabinet representatives and EOP staff.

Secretary Adams has proposed sweeping changes in ICC regulations of the rail industry, leading after a transition period, to virtually complete deregulation. We agree with the Secretary that major restructuring is necessary if we are to limit future federal involvement in this declining industry. We differ, however, on several details of the proposal.

In contrast to airline and truck deregulation, the immediate impact of rail deregulation is likely to be less service for many communities and higher rates for many commodities. We will argue that future federal outlays will be reduced, that the economic efficiency and health of the industry will be improved, and that trucks can more efficiently move much rail freight. But the political calculus will balance fears of short-term losses against hopes of long-term gains. Unlike the minor real impacts of the Amtrak cutbacks, freight railroad dislocations could affect large numbers of communities and workers.

To provide you with an overview this memo covers all major proposed reforms, and seeks your decisions on issues of controversy. There are six major areas in which Adams has made recommendations.

1. Rates

Adams Proposal

Secretary Adams has proposed a transition period of five years during which railroads would be free to raise or lower rates within a "zone of reasonableness." This zone would expand by 7% per year (in real terms) during the transition period. All rate regulation would cease after five years.

During the transition period railroads could apply to the ICC for authority to set rates even higher than the unregulated zone. These applications would be presumed to be approvable unless the shipper could demonstrate that he had no alternative way to ship his product. For these "captive" shippers faced with rate increases higher than the unregulated zone the ICC would continue to set rates.

The plan would also allow railroads and shippers to enter into long term contracts governing rates. These contract rates would be exempt from regulation.

Even though individual rates on various commodities would be deregulated within the zone, rail companies would still be subject to our inflation guidelines, possibly based on a modified profit margin test.

Discussion

Most concerns regarding this proposal center on the lack of protection provided to captive shippers, both within the "zone of reasonableness" and after the five year period ends. The Department of Energy, the Department of Agriculture, and CWPS for example, are greatly concerned with the probable increases in shipping costs that commodities like wheat and coal may face.

On the other hand, OMB and DOT are concerned that the 7% zone of reasonableness may provide too little flexibility in the short term to help the most troubled railroads, especially Conrail. They point out that for some weaker railroads two or three years of 7% increases may only bring them back to break even rate levels.

Decision Issues

There are two major issues for decision:

a) Should we propose total elimination of maximum rate regulation after the transition period ends, or allow the expanded zone to become a cap on unregulated rates, pending our evaluation of the results of the transition period?

DOT, CEA and OMB feel that complete rate flexibility is very important to the efficiency of the transportation system and the health of the rail industry. They argue that very few shippers are truly captive over the long term, and that these problems should be addressed by long term contract rates, mandatory switching rights, and unregulated new entry rather than by continued ICC regulation. While they concede that we may not win this issue in the Congress, they feel that we should position ourselves in favor of complete deregulation and accept modifications later.

We disagree. Along with many in the Congress, we are not convinced that contract rates and switching rights will be sufficient protection to captive shippers. An expanded zone (i.e., 35% above or below current rates) should effectively deregulate most commodities. If we recommend elimination of even this ceiling, shippers and communities will claim that they will face catastrophic rate increases in five years. Congress will argue that we are asking them to accept on faith our assumption that rate freedom will not lead to severe dislocations, rather than waiting to see the results of the transition period.

Decision

Eliminate maximum rate regulation after five years ✓ _______________ (DOT OMB CEA)

Leave ceiling in place pending results of transition _______________ (DPS CWPS)

J

b) How fast should the zone of reasonableness be expanded?

CEA feels that the zone should expand by 5% per year (plus inflation) up to a maximum of 25%. DOT and OMB have recommended 7% (plus inflation) zone expanding to 35%. There is little data on which to base a firm judgment. A lower level obviously creates fewer inflation problems. A higher level accomplishes the goals of deregulation earlier and more effectively. This could be especially important for Conrail. On balance we recommend that you propose the higher escalator. This will provide more room for negotiation with Congress, especially if, as we recommend, we freeze the unregulated zone after five years.

Decision

5% per year ______________ (CEA CWPS)

7% per year ______✓______ (OMB DPS DOT) J

2. Rate Bureaus

Adams Proposal

Adams recommends that we continue to grant limited anti-trust immunity to rate bureaus. Under the proposal the bureaus could continue to meet to set interline rates but could not discuss rates for single line shipments. In addition, Adams would prohibit the railroads from meeting collectively through rate bureaus to set general freight rate increases (i.e., percentage rate hikes for all commodities).

Discussion

Some agencies, such as Justice and FTC argue that rate bureaus should be abolished, consistent with our position on truck rate bureaus. Justice points out that even without the rate bureau anti-trust exemption there would be no anti-trust problem with two railroads meeting to discuss interline rates.

DOT argues, however, that the rate bureaus serve other useful functions such as setting industry-wide car rental rates and other standards. DOT feels that even if rate bureaus were abolished some mechanism for collective discussions would be needed to replace rate bureaus in this highly inter-dependent industry. They believe their proposal to limit the most anti-competitive activities of rate bureaus is a fair balancing of interests. If we proposed total abolition of the rate bureaus the railroads would be likely to oppose our bill strenuously. With the exception of the issue below we strongly agree with the DOT view.

Decision Issue

Should we provide for a transition period during which railroads would retain the right to set general rate increases through the rate bureaus?

For the past two decades the railroads have relied on general rate increases to cover their ever escalating labor and capital costs. The railroads have argued forcefully that until they have full rate freedom general freight rate increases are the only way they can keep up with inflation. They argue that if this protection against inflation is suddenly lost many railroads will be unable to adjust rapidly enough to the new environment and will be bankrupted. The Association of American Railroads feels so strongly regarding this issue that they have threatened to oppose (rather than just to seek modifications in) our bill if we refuse to allow general rate increases during a transition period. They argue that if our goal is truly to improve the health of the industry we should not immediately prohibit a practice on which the industry is so dependent. They propose that we allow a transition period during which the rate bureaus would still be able to establish general rate increases up to the amount of inflation. The size of these general rate increases could be phased down as the zone of price freedom phases up, with general rate increases prohibited when full deregulation takes effect.

DOT points out that the zone of price freedom covers <u>inflation plus</u> seven percent. Thus, any individual railroad would have the right to raise all its prices to cover inflation, and any two railroads would have the right to raise interline rates by an equal amount. They feel that it would be inconsistent for us to advocate a new era of pricing freedom while still supporting the most anti-competitive practice in the industry. They believe that general rate increases must be eliminated if the railroads are ever to develop a truly efficient and profitable price structure. While they are sympathetic to the transition problems that could result from the loss of general rate increases, they doubt that any wave of bankruptcies will result. They believe that if any transitional right to general rate increases is written into the bill it should be done by the Congress rather than by the Administration.

We are more sympathetic to the railroad's concerns. We recommend a <u>brief</u> (e.g. two years) transition period during which <u>limited</u> (e.g. the rate of inflation or less) general rate increases would be allowed. Virtually every railroad executive with whom we have spoken feels that without general rate increases their profitability could be severely harmed by our bill. For the weak railroads this could mean a wave of bankruptcies within 12-18 months. To insure the support of the railroads (who we hope will be our chief allies in Congress) we believe a transitional phase-out of general rate increases is justified.

Decision

Abolish rate bureaus entirely ____________________(DOJ FTC)

End general rate increases immediately ____✓____ (CEA OMB DOT CWPS) J

Allow general rate increases during a transition period ____________________ (DPS)

3. Discrimination

Adams Proposal

The anti-discrimination clauses of the IC Act prohibit railroads from charging different rates to different shippers or connecting carriers. Adams proposes to modify these restrictions to allow railroads greater freedom to charge different prices when costs or competitive circumstances vary.

Discussion

The discrimination statutes are designed to protect smaller shippers, competing carriers (especially barges) and competing ports. The DOT revisions would significantly change the long standing common carrier obligations of the railroads to equalize service to all shippers, ports and communities. This change will have particularly important potential impacts on midwestern barge operators, the Ports of New York and Boston and thousands of small shippers. It could be highly controversial.

Despite the potential political problems, however, all agencies agree that we should vigorously defend the new anti-discrimination language proposed by Adams. Limiting the scope of the discrimination statues is fundamental to our goal of relying on market forces to promote greater efficiency in rail transportation.

Approve ____✓____ (All Agencies) Disapprove ____________

J

4. Mergers

Adams Proposal

Adams proposes to transfer authority over railroad mergers from the ICC to the Justice Department's anti-trust division (i.e., the Clayton Act). The Clayton Act has a provision which exempts rail mergers and acquisitions when there is no substantial competition between the merging companies. This would have the effect of eliminating the prolonged hearing process (2-1/2 years) that currently must be undertaken by the ICC in every contested merger case. It would speed up and encourage "end-to-end" mergers.

Discussion

This change could promote a number of railroad mergers between connecting carriers. Because rail mergers frequently threaten the competitive circumstances of other railroads, this relaxation of merger prohibitions will be threatening to many railroads as well as to some shippers and communities.

We and other members of the EOP and the Executive Branch, however, believe that a freer environment for end-to-end mergers is an important tool to promote restructuring of the industry.

Approve ✓ (All Agencies) Disapprove ______

J

5. Abandonments

Adams Proposal

Adams recommends that the provisions of the 1976 4R act (which speeded up and somewhat relaxed ICC abandonment procedures) be retained for 3 more years. After that time a railroad would be permitted to discontinue service on 240 days notice unless a responsible party could offer a subsidy to cover the full cost of the service. After 3 additional years under these procedures, a railroad would have a right to discontinue service on 240 days notice regardless of whether a subsidy was offered.

Discussion

This proposal for virtually complete abandonment freedom in six years is likely to be the most controversial issue in the rail package. Rail abandonments go to the heart of the fears of railway labor, rural communities and small shippers. It is unlikely that a proposal as sweeping as this can be enacted. On the other hand abandonments are obviously important to our goal of rationalizing the nation's rail system, and may be crucial to improving the financial viability of many lines.

Decision Issue

Should the proposed DOT abandonment procedures be modified or implemented earlier?

Because abandonments are central to improved rail efficiency OMB and CWPS feel strongly that Adams' liberalized abandonment procedures should be implemented immediately rather than after a three year wait. They point out that the delay could cost the industry hundreds of millions of dollars annually and that these costs will be borne most heavily by the weakest railroads, especially Conrail. Further bankruptcies and the spector of a "Conrail West" are possible if the industry does not move aggressively to restructure itself. At the current rate of abandonment it would take 12-14 years to abandon the estimated 30-35,000 miles of uneconomic lines.

We view the situation in a different light. We believe that Congress will not significantly liberalize rail abandonment procedures because too many rural areas are potentially affected. For this reason we see no reason to incur gratuitous political criticism for the sake of stating an unrealizable philosophical goal.

This argument seems particularly persuasive because it appears that modest improvements in abandonment procedures may be all that is really needed. Currently the railroads are formally abandoning about 2,500 miles of track per year and are effectively abandoning (by failing to maintain) many thousands of miles more. Because so little investment is actually being made on many branch lines, the actual cost of continuing to serve these lines may be somewhat less than OMB estimates. Moreover, the rate freedom proposal we have made provides an avenue by which rates on these lines may be raised to help cut losses or even show profits.

Since the policy outcome is likely to be a limited revision of current ICC abandonment procedures we recommend that DOT be instructed to revise its legislative package to develop improvements in current law (to take effect immediately) rather than the complete abandonment rights currently proposed. For example, timetables for ICC procedures could be expedited and guidelines for abandonment approvals could be liberalized. These changes would effectively increase the rate at which abandonment could be approved by the ICC without requiring us to engage in a confrontation with Congress in which we would be in the position of advocating wholesale abandonments in 6 years.

Stu - Discuss your proposal with Brock - Let him make final decision. I don't understand the difference
J

Decision

Implement full abandonment freedom immediately no
(CWPS OMB)

Phase in full abandonment procedures over 6 years ?
(DOT CEA)

Modify current ICC abandonment procedures effective immediately
? (DPS)

6. Labor Protection

Adams Proposal

Secretary Adams has recommended that our bill call for labor protection provisions similar to those in the 1976 4R Act. These provisions would essentially protect workers against adverse impacts (especially wage losses) for up to six years after mergers or abandonments. By tradition, and in contrast to the recent airline bill, the railroads rather than the federal government bear the full cost of this protection. The one major change from past practice proposed by Secretary Adams would vest the power to approve labor protection agreements with the Department of Labor (DOL) rather than with the ICC as at present.

Discussion

These labor protection provisions appear to be the minimum necessary to satisfy railway labor. The unions, who are extremely influential in the House Commerce Committee, may seek more protection, and may oppose many of the key provisions of our bill in any case. But all EOP agencies urge that further concessions to the unions should wait until the legislative process is further advanced.

Approve ✓ (All Agencies) Disapprove ______

J

KAHN ATTACHMENT

THE WHITE HOUSE

WASHINGTON

March 6, 1979

MEMORANDUM TO THE PRESIDENT

FROM: Alfred E. Kahn Fred

SUBJECT: Rail Deregulation

I feel I must emphasize more clearly than I think appears from the memorandum of issues, to what extent your anti-inflation and energy policies dictate your choice of the 5% rather than the 7% zone of discretionary price increases, the re-examination rather than simple deregulation of pricing at the end of five years, and the prohibition of general rate increases.

In each case, please observe that my concern arises out of the fact that we are not here simply substituting effective competition for regulation, but opening up the possibility of exploitation of captive shippers by a monopoly carrier from whom they have no ready escape.

The relation to your energy policy is that some of the railroads have already sharply increased rates for the carriage of coal, shippers of which in many instances have no ready alternative; and this will make more difficult the coal conversion program.

On the question of general rate increases, it seems to me that if we are going to give the railroads substantially greater pricing freedom, on both the up and the down side, we have a right to withdraw the antitrust exemption for collective rate-making.

CL ATTACHMENT

THE WHITE HOUSE

WASHINGTON

March 6, 1979

MEMORANDUM TO: LES FRANCIS/RICK HUTCHESON

FROM: BOB THOMSON

SUBJECT: EIZENSTAT MEMO REGARDING RAIL DEREGULATION

We have consulted with Senate staff members in the absence of their principals at the Bartlett funeral. In general and as is always the case, they recommend a cautious approach. They prefer leaving ceilings in place after five years, a transition period for termination of rate bureaus, and a modest modification of abandonment rules. Significantly, there was no objection to doing away with discrimination statutes and no recommendation as to how fast the zone of reasonableness should increase.

For tactical reasons, I recommend that the President take the more extreme position on some of these issues, and let Congress compromise if compromise is needed to pass the bill.

For example, the President could propose the more rapid expansion of the zone of reasonableness and the more immediate implementation of liberalized abandonment. However, we should not follow this philosophy with rate bureaus and the post-transition period ceiling. Those issues are too central to rail deregulation for them to be tactical pawns. On these latter two issues, we share the view of the Domestic Policy staff. However, regarding rate bureaus, we could live with DOT's option.

~~CONFIDENTIAL~~

THE WHITE HOUSE
WASHINGTON

3/7/79

Zbig Brzezinski

The attached was returned in the President's outbox today and is forwarded to you for appropriate handling.

Rick Hutcheson

cc: Jim McIntyre

MEMORANDUM

THE WHITE HOUSE

WASHINGTON

1453

~~CONFIDENTIAL~~

March 7, 1979

ACTION

MEMORANDUM FOR: THE PRESIDENT

FROM: DAVID AARON

SUBJECT: Certification on Yemen Arms Sales (U)

On March 8, 1979, formal certification will be made to Congress of the following sales to North Yemen:

12	F-5 aircraft
64	M60 tanks
50	M113 Armored Personnel Carriers. (C)

These sales were approved by you some time ago and were informally notified to Congress twenty days ago. (U)

Section 36 of the Arms Export Control Act requires that proposed major sales lie before the Congress for thirty calendar days unless the President waives that requirement by certifying that "an emergency exists which requires such sales in the national security interests of the United States." Since section 36 was added to the Act in 1974, no such certification of emergency has been made. (C)

Delivery of the items for the YAR, which could begin within 72 hours of signature of the letter of offer and acceptance, will be delayed for 30 days unless the provision is waived. If these items are to be of any real assistance in the current fighting, delivery must be accelerated. (C)

RECOMMENDATION:

That you sign the certification at Tab A and approve its inclusion with the formal certification of these sales to the Congress. This is required to implement the decision of the NSC in which you participated on Monday.

Cy and DOD concur.

Approve ✓ __________ Disapprove __________

~~CONFIDENTIAL~~
~~Review on March 7, 1985~~

THE WHITE HOUSE

WASHINGTON

Presidential Determination
No. ______________________

MEMORANDUM FOR:

THE SECRETARY OF STATE
THE SECRETARY OF DEFENSE

SUBJECT: Sales of Defense Articles and Defense Services Under the Arms Export Control Act to the Yemen Arab Republic

In accordance with section 36(b)(1) of the Arms Export Control Act (the Act), I hereby certify that an emergency exists which requires the sale under the Act of the following defense articles and defense services to the Yemen Arab Republic in the national security interests of the United States:

- 12 F-5E aircraft
- 64 M60-A3 tanks
- 50 M113-A1 Armored Personnel Carriers
- Related support, spares, training and munitions for the above systems.

This certification shall be made part of the certification transmitted to the Congress under section 36(b)(1) of the Act with respect to each of the above sales, and shall be published in the Federal Register.

Jimmy Carter

THE WHITE HOUSE

WASHINGTON

March 2, 1979

MEMORANDUM FOR: THE PRESIDENT

FROM: STU EIZENSTAT Stu
BOB MALSON B.

SUBJECT: Conglomerate Merger Proposal

Last month you reviewed our memorandum outlining the Justice Department's conglomerate merger proposal and the preliminary responses of the interested departments and agencies. You chose not to decide the issue, at that time, and in a note to the Attorney General you stated your desire to obtain the considered views of the agencies by February 15 before deciding whether to support the proposal. This memorandum does not repeat the proposal or the arguments we described in our January 21 memorandum. Rather, we have focused on the departments and agencies comments and the pros and cons.

Horizontal mergers (between competitors) and vertical mergers (among suppliers, manufacturers and sellers in a linked production and marketing chain) which would retard competition can be dealt with under existing antitrust laws. Those laws, however, have been interpreted not to prevent conglomerate mergers -- that is, acquisition by one company of another in a totally unrelated market where competition data is unavailable and generally stated in subjective, predictive terms. Justice believes that conglomerate mergers may have, in some instances, anti-competitive effects; that mergers between very large corporations should be permitted only if they would promote competition; and that the burden of proof should be on the companies seeking to merge. Justice believes these new standards are necessary because conglomerate mergers lead or could lead to increasingly larger concentrations of economic power which are undesirable politically and socially.

The Attorney General has submitted the attached memorandum which emphasizes four points.

- The number of mergers exceeding $100 million purchase price increased from 14 in 1975 to 80 in 1978;

V

- o <u>Treasury</u>: "...while the DOJ lists the possible adverse social and political effects of conglomerate mergers, it does not demonstrate that these are substantial concerns.... We do not believe that the social and political concerns often attributed to conglomerate bigness have been clearly diagnosed, and, in view of the comments made below, we question whether these concerns would be well served by the DOJ proposal.... The DOJ paper asserts that (1) the operation of large conglomerate firms have anticompetitive consequences for particular markets, and (2) limiting conglomerate mergers by large firms is procompetitive.... Neither of these points is adequately supported in the paper and we question whether either is substantially correct.... In fact, to our knowledge available studies do not indicate that conglomerate mergers have anticompetitive effects." The DOJ January 29 paper presented thirty indices of trends in aggregate concentration in the U.S. Treasury responded to the statistical case: "Most of the series presented by DOJ do <u>not</u> indicate a trend towards overall concentration. On the contrary, they indicate no change in aggregate concentration or a decreasing trend.... It is, finally, important to recognize the limited role played by mergers in any trend towards increased overall concentration in U.S. industry.... Consequently, even assuming that it is possible to make a case that bigness <u>per se</u> is bad, there would seem to be no compelling reason to focus on acquisitions as opposed to other trends."

- o <u>Commerce</u>: "The proposals by the Justice Department, the Federal Trade Commission, and the staff of the Senate Judiciary Committee to impose additional constraints on conglomerate mergers have not matured to the point of Presidential decisionmaking. Indeed, the concentration problem has not been verified. The economic, social or political implications of the proposed solutions are scarcely examined.... If bigness cannot be linked directly to actions that undermine our economic, social or political institutions, then legislation should not be used to bound firm size.... <u>Justice not only fails to document the anti-competitive effects of conglomerate mergers, it also proposes a solution--size constraint--which constitutes a significant departure from long-standing policies and which does not address their anti-competitive concerns</u>.... (emphasis by Commerce) The Department of Justice claims that large conglomerate mergers have had adverse effects on small communities. It is not clear from empirical evidence whether these adverse effects have occurred; moreover, even if one accepts the premise that there have been some dislocations, the solution proposed by Justice--a major revision in our antitrust laws--is out of proportion to the problem." Commerce concluded by stating that a decision to ban mergers should be based on a careful analysis of the economic, social and political costs and benefits and quoted Assistant Attorney General Shenefield's July 1978 testimony before the Senate Antitrust Subcommittee. He called then for "...more data and analysis concerning the motives for mergers, their role in increasing aggregate concentration, the effects of such acquisitions on acquired companies and the adverse effects of restricting certain types of mergers." Commerce believes these studies are necessary before proceeding with conglomerate merger legislation.

Political Costs and Benefits

The arguments for supporting some limitation on conglomerate mergers are:

1. It is a tradition of the Democratic Party to seek to limit the power and influence of big business. Senator Kennedy will submit a bill and hold hearings and we may be criticized in traditional liberal Democratic circles if we do not favor the concept.

2. There is a fair amount of concern in the country generally about the wave of mergers. Ordinary citizens are likely to support the idea.

3. The AFL-CIO passed a resolution at Bal Harbour this past weekend supporting legislative efforts to curb conglomerate mergers.

4. Small business, through the National Federation of Independent Business, has expressed interest in supporting some legislation in this area.

Arguments against:

1. The economic evidence is at best neutral so that we are likely to be left with the "bigness is bad" justification.

2. The bill is not likely to pass this session. Beyond Kennedy, it is not at all clear that there is great interest or support elsewhere in the Senate or in the House.

3. The Business Roundtable met with us last month and stated that there is no credible support for new anti-merger legislation. While the Antitrust Division and the FTC are experts in the antitrust fields. "...they do not possess any special expertise with respect to broad social policy issues. Hence their judgment on social policy issues cannot be accepted without credible support."

   The National Association of Manufacturers asks that you not take a position before interested persons have an opportunity to set forth their views at next month's Senate hearings. They wish to question the proponents as to the benefits they claim will accrue to the nation as a result of efforts to dramatically reform existing merger doctrines. Specific questions NAM intends to raise are:

   - Would a ban on large mergers stimulate large firms to acquire small and medium-size companies?
   - Would a ban on large mergers (and their efficiencies) have a significant inflationary impact?
   - What are the proponents' views of the impact of the proposal on the ability of the United States to compete in world markets?

   NAM believes that following the Senate hearings you can best answer whether modifying the anti-trust law is the appropriate way to accomplish social reforms which bear little or no relationship to competition policy.

   The cooperation of the business community is essential if the Administration's anti-inflation program is to succeed; that cooperation should not be jeopardized over a proposal which responsible opponents will contend rests upon dubious economic and social arguments.

4. The legislation, as drafted, provides a distinct advantage to foreign corporations. There does not appear to be a satisfactory way to avoid this effect.

Options

There are four basic options available to address the issue:

1. Approve the DOJ proposal and authorize the Attorney General to try to work out a bill in conjunction with Congressional leaders.

2. No Administration bill but allow the Justice Department, on behalf of the Administration, to testify in favor of Senator Kennedy's bill. We would seek to avoid having unsympathetic agencies testify.

3. No Administration bill but allow the Justice Department to testify on behalf of the Kennedy bill, while permitting other agencies to state their views. There would be no Administration position at this time and interested departments could contribute their views to the dialogue.

4. Oppose all conglomerate merger legislation.

The strong differences of opinion within the Administration on this subject are fundamental and philosophical. Assistant Attorney General Shenefield has taken public positions in favor of the concept for months. We have been informed that he would decline to testify against an anti-merger proposal.

But the Justice proposal is more than an antitrust measure-- it would have a substantial impact on business and the economy in the U.S. as well as abroad. The views of State, Commerce and Treasury would be appropriately requested. These departments have raised the tough questions they would be expected to answer and their testimony could hardly be expected to be very supportive.

We agree with Justice that unfettered conglomerate mergers are likely, over time, to be harmful to the Nation. While the economic arguments can be made on either side of this issue, it is difficult to argue that conglomerate mergers are good for the country. The Justice proposal does not ban such mergers but creates a higher burden of proof to sustain them than now exists.

We see no reason why the Attorney General or his department should not be permitted to generally endorse legislation introduced by the Committee Chairman, Senator Kennedy, with whom they must deal on so many issues. Also, it is politically advantageous to have Kennedy with the Administration on as many issues as possible -- and vice versa.

Decision

1. ________ Approved. The Attorney General is authorized to proceed with his proposal to send to the Congress the Justice Department's draft merger legislation. (Justice, FTC, ICC, SBA. DOT agrees, but only if railroads, airlines and the trucking industry are exempted by statute and if deregulation issues are resolved; DPS fall-back)

2. ________ Approved. Administration support for merger limitation but no separate bill is to be submitted. Justice is authorized to testify in favor of merger legislation and to speak for the Administration on the subject of conglomerate mergers. (DPS, Wexler)

3. ________ Approved. No Administration bill but allow the Justice Department, to testify on behalf of the Kennedy bill, while permitting the agencies to state their views. There would be no Administration position at this time and interested departments would contribute their views to dialogue. (OMB)

4. ________ Approved. The DOJ proposal is rejected. The Administration should oppose legislation to restrict conglomerate mergers. (Commerce, Treasury, Labor, State, CEA)

JUSTICE MEMO

Office of the Attorney General
Washington, D.C. 20530

21 FEB 1979

MEMORANDUM TO THE PRESIDENT

Re: Legislative Options on the Problem of Conglomerate Mergers

In January you reviewed our Justice Department proposal to seek legislative tightening of the merger laws, and gave other agencies until February 15th to study the proposal prior to your making a decision. To assist, we circulated a 72-page analysis of the social, political and economic problems of giant conglomerate mergers, and included all of the data series on merger trends and aggregate concentration that were available; the "Executive Summary" is attached.

Four essentials can be distilled from our study: (1) The number of large mergers (involving a purchase price of $100 million or more) has dramatically increased in the past few years -- e.g. going from 14 in 1975 to 80 in 1978, with no reason to expect a downturn in this trend. (2) Present law, which requires the government to prove adverse competitive effects in particular markets, does not allow us adequately to scrutinize most of the giant mergers since they are conglomerate in nature -- i.e. the two companies do not have overlapping activities in product or geographic markets. (3) The adverse social, political and long-term economic effects of a continued trend of giant mergers are widely perceived as compelling reasons for subjecting giant mergers to effective legal scrutiny. (While reasonable men within the Administration differ as to how much weight to attach to various factors, such as whether aggregate concentration is increasing across-the-board or only in key sectors like manufacturing, there is no doubt that the concerns about giant mergers are genuine). (4) The issues are already on the nation's agenda, with both the Senate and House Judiciary Committees committed to activity on conglomerate mergers early in this Session of the 96th Congress. (The House Committee on Small Business recommended in the last Congress that proposals be developed "to reverse the trend toward increasing aggregate concentration through mergers and acquisitions"). The Senate Judiciary Committee has scheduled hearings on March 6, 1979. Consequently, Administration spokesmen will necessarily have to respond.

The dialogue within the Administration within the past few weeks has strengthened my belief that legislative action is required. I strongly believe that we should ourselves take the initiative (in cooperation with Congressional leaders, which we believe will be possible), in presenting a well-structured proposal around which debate can responsibly be focussed.

The Justice Department proposal would basically change the law's presumption on defined classes of very large mergers, so as to make proponents of a very large merger prove that the preponderant effect will be substantially to enhance competition (rather than requiring the government to prove that the merger may substantially lessen competition in a particular market). Precise coverage, and precise ways in which businesses proposing desirable mergers can prove their case can be further refined in the legislative process; our proposal is not designed to forestall further debate. However, the basic outline -- presumptive illegality of mergers of large firms with one another and with leading firms in concentrated markets, with allowance for proof of positive benefits -- is, I believe, worthy of endorsement.

Thus, I urge you to approve our proposing essentially the Justice Department bill, if possible in cooperation with Congressional leaders, early in the 96th Congress.

Respectfully,

Griffin B. Bell

Griffin B. Bell
Attorney General

LARGE CONGLOMERATE MERGERS

An Analysis and a Proposal

Executive Summary

Large conglomerate mergers (i.e. the joining of firms producing different products) and the aggregation of economic power reflected by them continue to trouble responsible minds and will be the subject of legislative activity in the 96th Congress. They are widely perceived by the public as undesirable, based on the adverse social and political effects of increased aggregate concentration, and on concern over possible long-term economic effects as well. Most conglomerate mergers are beyond the reach of the present merger law.

The problem is now underscored by a resurgence of conglomerate merger activity. The number of mergers involving a purchase value of more than $100 million totalled 80 in 1978, compared to 41 in 1977, 39 in 1976, and 14 in 1975. During 1977, mergers by manufacturing and mining firms with assets of over $1 billion totalled 28 and involved total assets of $4.659 billion, compared with 18 such mergers in 1976 involving total assets of $2.530 billion. In the last decade, 1968-1977, industrial firms with more than $1 billion in assets acquired 160 enterprises in conglomerate mergers, with the acquired firms averaging $130 million in assets. In recent years, conglomerate mergers have represented 80 to 90 percent of merger activity by asset size, contrasted with only 38 percent in 1950.

Large conglomerate mergers are viewed as socially and politically undesirable because they concentrate power in the hands of the few corporate managers of the conglomerate empires, remove corporate headquarters or control from smaller cities to larger ones, and make companies more impersonal and less responsive to the specific needs of particular markets.

Aggregate concentration of economic power in our country, measured by a number of different yardsticks, has not diminished since World War II, but rather continues its long-term upward trend. Large conglomerate mergers clearly accentuate the problems of aggregate concentration; about 13 percent of the total assets of 1975's top 200 industrial companies represented assets acquired by mergers.

There is also considerable evidence that many large conglomerate mergers are not based on any expected efficiencies or synergism, but simply reflect the financial attractiveness of the transaction at a given stock or asset price, or the desire of management to use surplus funds to acquire existing companies rather than invest in new plant and equipment or distribute the funds to stockholders. Finally, while there is no consensus, many antitrust lawyers and economists continue to believe that large conglomerate mergers will produce long-run anticompetitive effects by lessening the number of firms that might become significant potential competitors to each other, creating a mutual interdependence of firms that meet each other in many markets, and increasing the possible financial barriers to entering markets to compete against the participating firms. The difficulty is in proving such effects in individual markets, as is now required under current merger law.

In 1976, Congress evidenced continuing concern about mergers by enacting the pre-merger notification statute, affecting transactions in which firms with assets or sales of over $100 million acquire other firms with assets or sales of over $10 million. Notification to the Justice Department and Federal Trade Commission, however, does not change the substantive standards of Section 7 of the Clayton Act -- under which most conglomerate mergers cannot successfully be challanged.

In the 96th Congress, it is clear that both the Senate and House Judiciary Committees will consider new legislation directed at conglomerate mergers. (In the 95th Congress, Senator Kennedy held hearings and Chairman Rodino commissioned a study of conglomerate mergers.) Senator Kennedy has made clear his intent to introduce legislation early in the 96th Congress (probably a total ban on all mergers over a certain size), but has also asked to work out a joint proposal with the Administration if an Administration bill is approved. Proposals will range from an outright, total ban on mergers among and by the "Fortune 500" or some portion of them, on the one extreme, to proposals for minor tinkering with the government's burden of proving anticompetitive effects in particular markets, on the other. Some, of course, will argue that no change should be made in the current law on the grounds that there is no definitive proof of specific harm from conglomerate mergers, that incumbent managements need the threat of takeovers to remain efficient, and that philosophically no restrictions should be placed on the flow of capital.

The Department of Justice believes that the conglomerate merger problem requires new legislation, and proposes a "middle-ground" statute that it believes can achieve the support of congressional leaders if backed early by the Administration as part of a joint effort.

The Justice Department's proposed statute would change the law's presumption so as to make proponents of a merger of very large firms prove that the preponderant effect of the merger will be to substantially enhance competition (rather than requiring the government to prove that the merger may substantially lessen competition). Two classes of transactions would be affected by the proposed statute: (1) large firms whose combined sales or assets would total $2 billion or more; and (2) any firm with $1 billion or more in assets or sales if it wishes to acquire a leading firm (20 percent or more of net sales) in a sizeable and concentrated relevant market (a market with $100 million or more of sales in which the four-firm concentration ratio exceeds 75 percent). To address the problem of foreign firms doing business in the United States, the statute would provide that a majority of the leading firm's assets must be located in the United States.

The basic theory of the Justice Department's proposal is to deter transactions of the defined classes unless they have a positive effect on competition and thus a positive effect in the long-run for consumers, and not continue to permit them for the short-term benefit of the companies involved, with no requirement for proof of socially and economically desirable results. In the broadest sense, the rationale is that our largest companies should be diverted from attempting to acquire one another and from attempting to acquire the leading firms in highly concentrated industries, thus potentially releasing their energies into more economically and socially desirable areas.

The proposal's effect can be seen using 1977 assets and sales data: unless the preponderant effect would be substantially to enhance competition, the 128 largest industrials (ranked by sales) could not acquire any firm with sales or assets of more than $100 million and the 242 largest industrials could not merge with larger firms. Similarly, the 40 largest retailers (in sales), the 47 largest diversified-financial companies (in assets), and the 45 largest life-insurance companies (in assets) could not merge with larger firms without proof of a positive effect on competition. Moreover, without such proof, none of these firms could acquire a leading firm in a sizeable concentrated market.

Over the past 30 years, the proposed statute's combined-asset provision (if it had been in effect) would have challenged only about 5 percent of the large merger transactions, but would have dealt with about 29 percent of the assets acquired in manufacturing and mining mergers. During the years 1975-1977, the combined-asset provision would have affected at least 32 mergers involving asset acquisitions totalling $19.2 billion. In short, the proposed statute has a responsibly narrow focus.

While the Department of Justice believes that the proposed statute is a sound first draft of timely conglomerate merger legislation, it is not intended to foreclose debate on such details as precise dollar figures, the appropriate showing which must be made to overcome the presumption of illegality, periodic adjustment of size criteria, etc. However, the basic outline of the statute -- presumptive illegality of mergers of large firms with one another and with leading firms in concentrated markets, with allowance for proof of positive benefits -- is, we believe, worthy of endorsement.

INTERNAL REVENUE SERVICE DATA

ALL INDUSTRIES

Percent of Total Corporate Assets and Receipts Accounted for by the 50, 200, 500 and 1,000 Largest Corporations for Selected Years

	1968	1974
ASSETS		
50 Largest	20.8%	23.1%
200 Largest	34.3	36.9
500 Largest	45.9	48.6
1,000 Largest	54.5	57.6
TOTAL RECEIPTS		
50 Largest	15.5%	19.2%
200 Largest	26.4	30.8
500 Largest	35.2	40.6
1,000 Largest	41.8	47.3

SUMMARY OF OTHER CATEGORIES	CONCENTRATION IN 1974 COMPARED TO 1968	
	ASSETS	RECEIPTS
All Industries	up	up
All Industries Less Finance, Insurance & Real Estate	up	up
Finance, Insurance & Real Estate	up	up
Manufacturing	up	up
Mining	up	up
Wholesale & Retail Trade	up	up
Transportation	up	up
Services	up	down
Agriculture, Forestry & Fishing	down	down
Construction	down	down

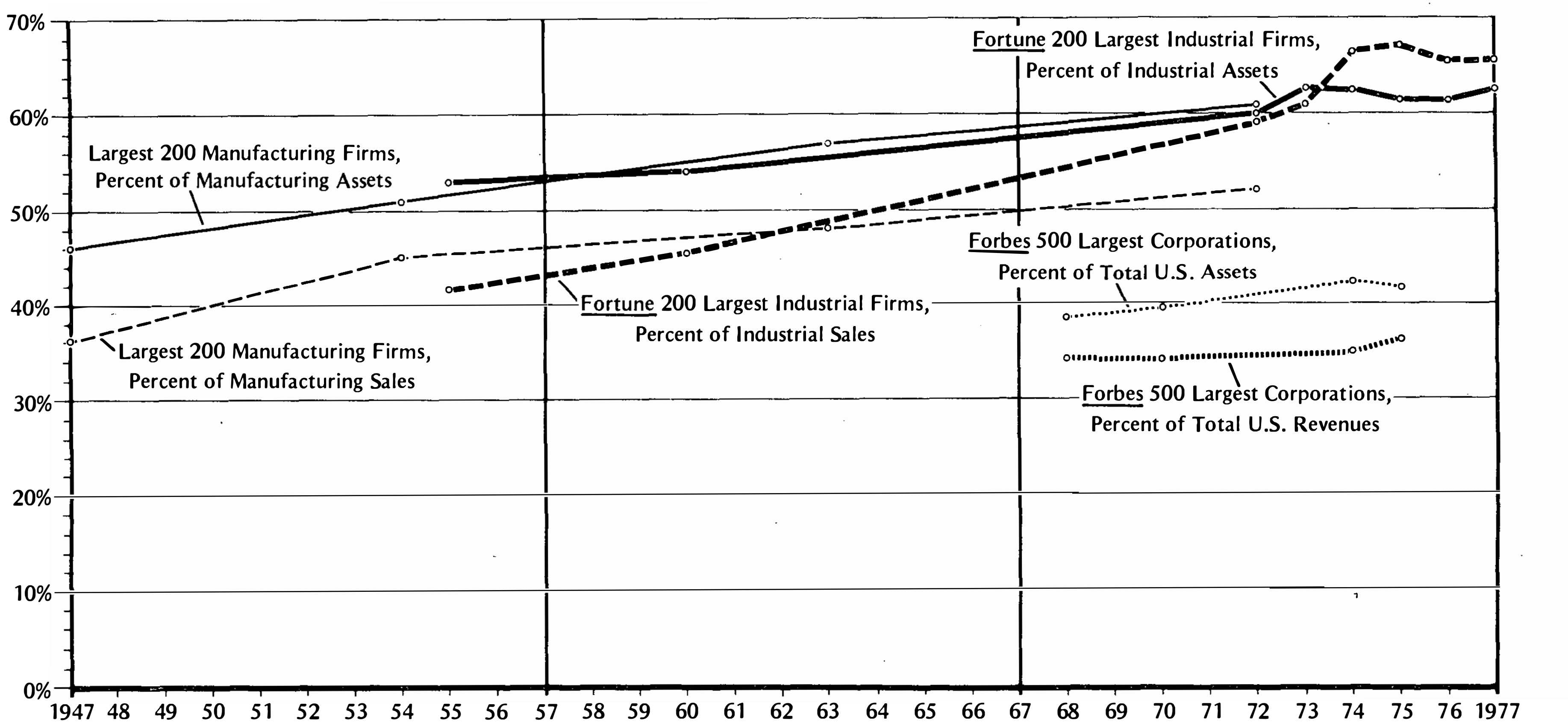
BUREAU OF THE CENSUS DATA

Share of Value Added Accounted for by the 50, 100, 200, 500 and 1,000 Largest Companies

	1947	1954	1962	1967	1972	1976
50 largest	17%	23%	24%	25%	24.5%	24.4%
100 largest	23	30	32	33	33.1	33.5
200 largest	30	37	40	42	43.1	44.0
500 largest					56.1	57.6
1,000 largest					64.4	66.1

CHART D

TRENDS IN AGGREGATE CONCENTRATION, BY VARIOUS MEASURES



Source: Justice Department Tables Based on Data from Various Sources.

CHART D

CHART D, Page 2

AGGREGATE CONCENTRATION BY ADDITIONAL MEASURES

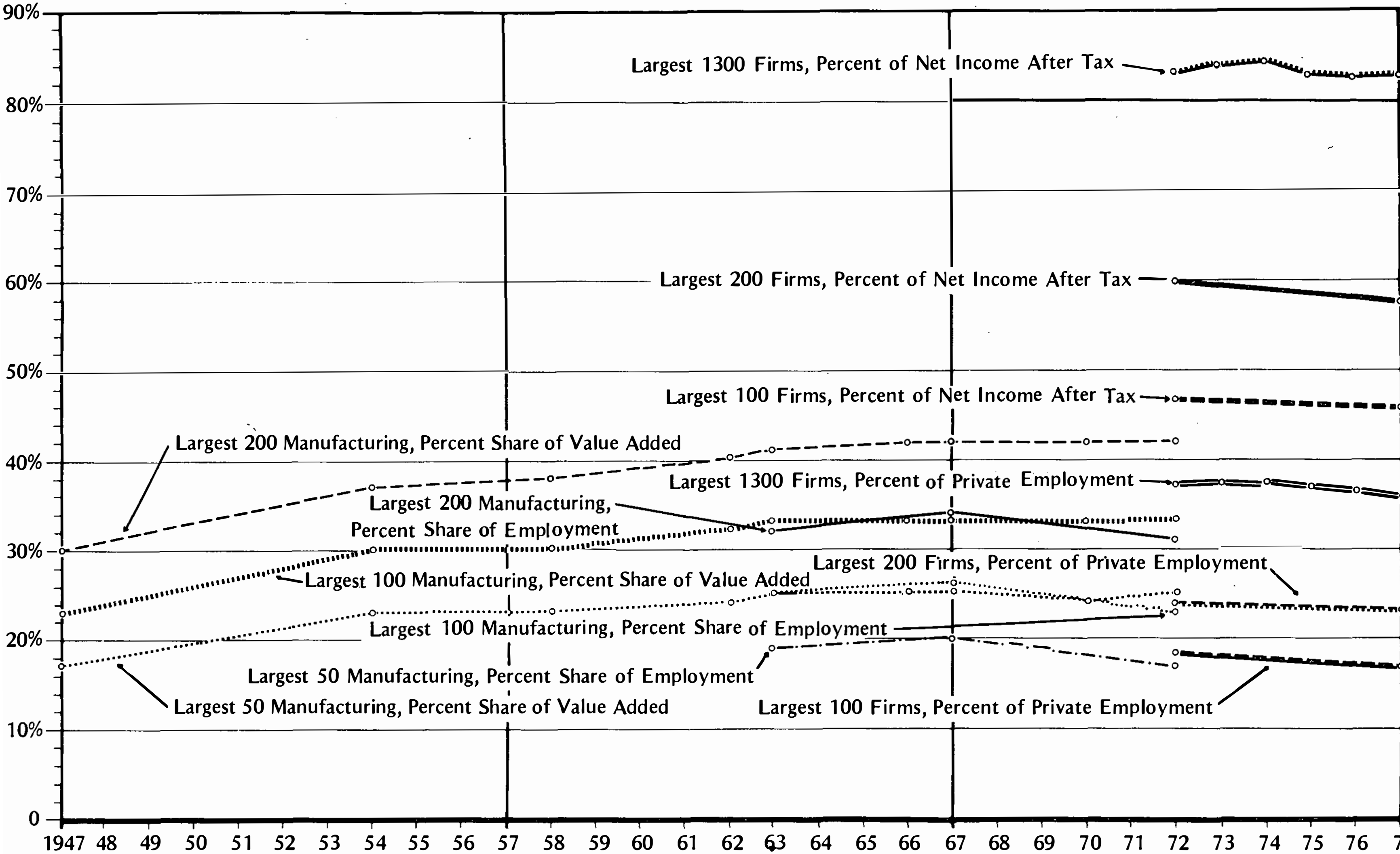


CHART D, Page 3

AGGREGATE CONCENTRATION BY ADDITIONAL MEASURES

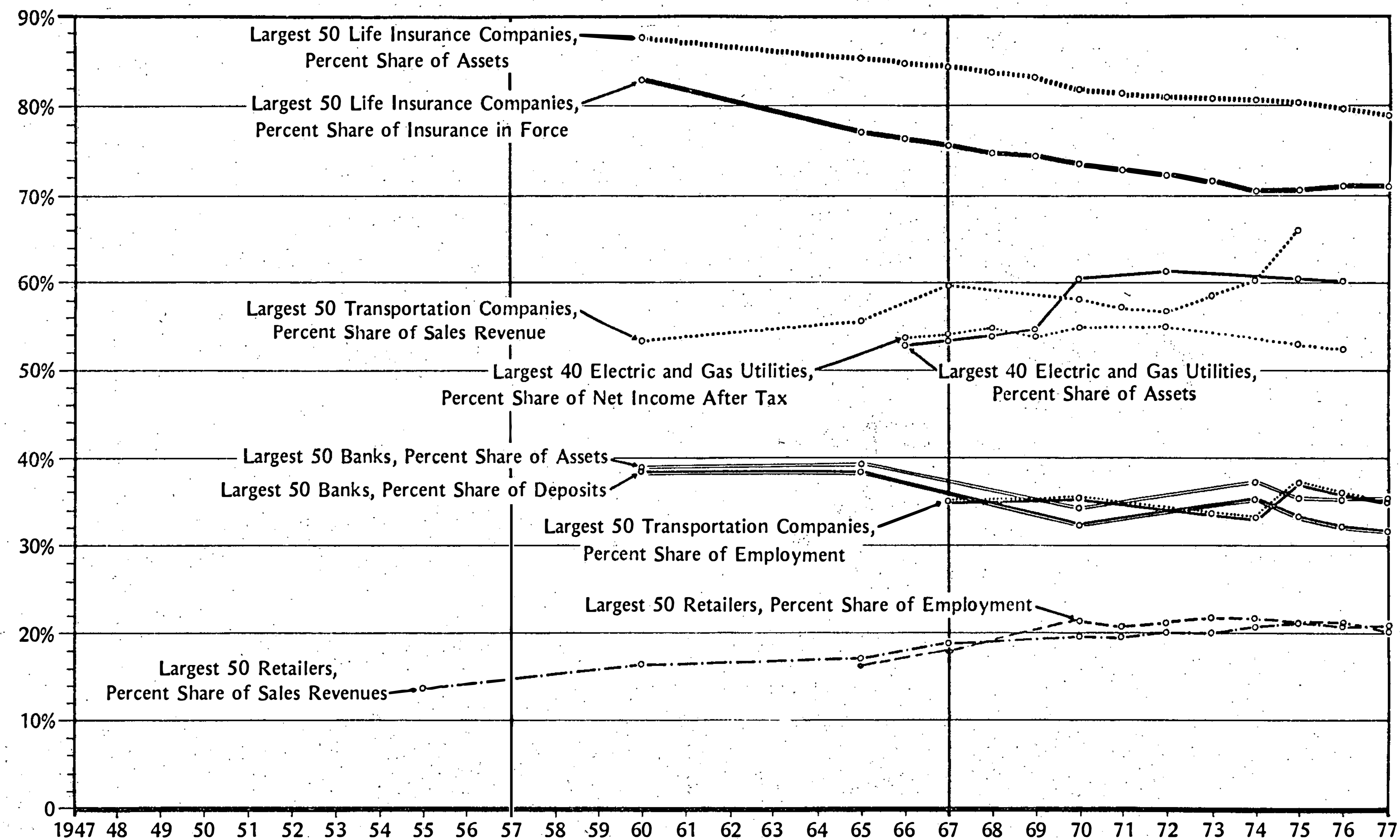


CHART D, Page 3

THE WHITE HOUSE
WASHINGTON

MARCH 6, 1979

SUSAN

STU EIZENSTAT WANTS YOU TO ASK THE PRESIDENT TO PLEASE COMPLETE THE MERGER MEMORANDUM BEFORE LEAVING ON THE TRIP BECAUSE KENNEDY IS HOLDING HEARINGS ON THURSDAY.

NELL

THE WHITE HOUSE
WASHINGTON

3/2/79

Mr. President:

No comment from Kahn or CL.

Rick

LM

THE WHITE HOUSE

WASHINGTON

3-7-79

To Griffin Bell

I'm not ready to set an administration policy re corporate mergers. The foreign competition issue, possible need for exemptions in transportation, utility and other industries, inadequate proof of effect on competition, how best to define thresholds and other questions require more analysis. Congressional hearings can, perhaps, provide some more answers.

You may testify favorably if you make it clear that I have not decided on a final policy. Other administration officers will also be permitted to testify independently under the same restraint.

This is the best I can do for now.

Jimmy

cc: Stu & others

	FOR STAFFING
	FOR INFORMATION
✓	FROM PRESIDENT'S OUTBOX
	LOG IN/TO PRESIDENT TODAY
	IMMEDIATE TURNAROUND
	NO DEADLINE
	LAST DAY FOR ACTION

FOR ACTION	FYI	
		VICE PRESIDENT
		JORDAN
	✓	EIZENSTAT
		KRAFT
		LIPSHUTZ
		MOORE
		POWELL
		RAFSHOON
		WATSON
	✓	WEXLER
		BRZEZINSKI
	✓	MCINTYRE
	✓	SCHULTZE
		ADAMS
		ANDRUS
✓		BELL
		BERGLAND
		BLUMENTHAL
		BROWN
		CALIFANO
		HARRIS
		KREPS
		MARSHALL
		SCHLESINGER
		STRAUSS
		VANCE

		ARONSON
		BUTLER
		H. CARTER
		CLOUGH
		CRUIKSHANK
		FIRST LADY
		HARDEN
		HERNANDEZ
		HUTCHESON
		KAHN
		LINDER
		MARTIN
		MILLER
		MOE
		PETERSON
		PETTIGREW
		PRESS
		SANDERS
		WARREN
		WEDDINGTON
		WISE
		VOORDE

	ADMIN. CONFIDEN.
	CONFIDENTIAL
	SECRET
	EYES ONLY

JANUARY 21
EIZENSTAT MEMO

ID 786619

C

THE WHITE HOUSE

WASHINGTON

January 21, 1979

MEMORANDUM FOR: THE PRESIDENT

FROM: STU EIZENSTAT Stu
BOB MALSON B.

SUBJECT: Conglomerate Merger Legislation Proposed by the Department of Justice

The Attorney General has submitted the attached legislative proposal to curb conglomerate mergers by the nation's largest corporations and asks that you (1) approve its introduction and (2) announce your support in the State of the Union message.

Horizontal mergers (between competitors) and vertical mergers (among suppliers, manufacturers and sellers in a linked production and marketing chain) which would retard competition can be dealt with under existing antitrust laws. Those laws, however, have been interpreted not to prevent conglomerate mergers -- that is, acquisition by one company of another in a totally unrelated market where competition data is unavailable and generally stated in subjective, predictive terms. Justice believes that conglomerate mergers may have, in some instances, anti-competitive effects; that mergers between very large corporations should be permitted only if they would promote competition; and that the burden of proof should be on the companies seeking to merge. Justice believes these new standards are necessary because conglomerate mergers lead or could lead to increasingly larger concentrations of economic power which are undesirable politically and socially.

Economic Considerations

Conglomerate mergers which may have an anti-competitive effect are presently unlawful under Section 7 of the Clayton Act. But it is virtually impossible to prove the anti-competitive effect of the merger of firms in unrelated markets unless there is strong evidence of potential competition; i.e., that one of the firms was a potential entrant into one or more of the other firm's markets.

The Justice Department believes that the trend towards aggregate concentration of wealth and power is clear and should be curtailed without regard to the Government's ability to prove anti-competitive effects. If, in the future, the anti-competitive effects of conglomerate mergers can be proven under current law, the economy would most likely already be under the control of a small number of corporate managers. Such vast economic power, if it is to exist at all, should rest in the hands of elected officials.

Critics of the proposal (1) dispute the theory; (2) argue that the proof is inconclusive whether conglomerate mergers have an effect on compeition; and (3) believe the data on aggregate concentration is very mixed -- increases and decreases abound in different segments of the economy and vary depending upon the time period. The major elements of the economic discussion are:

- <u>Competition</u>: Little evidence exists that conglmerate mergers have affected competition. There is agreement on this point between those who propose anti-conglomerate merger legislation (Justice, FTC and Kennedy) and opponents (CEA, OMB, Commerce and Treasury).

- <u>Aggregate Concentration:</u> Justice states that merger acquisitions since 1948 have involved cumulative assets of 13.6% of the 200 largest manufacturing and mining companies. (Only a portion of that percentage was due to conglomerate mergers.) Justice argues that overall concentration has had a continuing upward trend over the last 35 years. Treasury counters that mergers occur in waves (we are in the third merger wave of this century) and overall concentration in the entire economy has been declining since 1972. It would appear that any increase is marginal over time. The evidence is cloudy on whether conglomerate mergers have contributed substantially to an increase in concentration.

- <u>Diversion of Funds:</u> It is alleged that conglomerate mergers divert corporate funds from productive investment in their own industries to buying up firms in other industries. This assertion is unsupported by evidence and we do not know what alternative options management would choose if conglomerate mergers were banned.

- o **Market Allocation of Resources:** Enactment of the proposal might remove some of the competitive discipline of financial markets (applicable to the affected mergers) from the economy without a finding of a market failure.

Social and Political Considerations

Given the neutrality of the economic evidence, the social impact must be considered as the principal basis for anti-merger legislation.

"Bigness is bad" is the euphemism generally used to describe the common perception that it is not in the national interest to have huge concentrations of wealth and power in the hands of few people. This perception has a long history in the Nation's politics and thought but its elements are difficult to quantify and measure and thus are beyond the scope of the generally accepted instruments used by economists, financial analysts and antitrust experts who tend to dominate the scholarship in the field. The concept, in the final analysis, is both social and political in nature and its elements are:

- o The lawful ability to concentrate economic power will breed anti-democratic political pressures.
- o The range within which private discretion by a few in the economic sphere control the welfare of all should be limited.
- o The free market sector of the economy should not be allowed to develop under antitrust rules that are blind to all but economic concerns.

Here the proposed remedies are not aimed at all firms above a given size. Rather, the proposals under review are targeted at large firms which seek to become larger through a particular mechanism -- mergers. Internal growth would not be precluded.

Proposed Remedies

- o The Justice Department would prohibit the merger of firms whose combined assets and sales exceed a stated size unless it could be proven that competition would be substantially enhanced. Two alternative tests are involved:

THE WHITE HOUSE
WASHINGTON

Rafshoon comment on att. General memo due today:

"Fine for Judge Bell but President should not be up front on this"

(1) All corporate mergers exceeding $2 billion in combined sales and assets would be affected. This test is aimed solely at the size of the new entity and is designed to block the largest mergers.

(2) Acquiring firms with $1 billion in combined sales and assets would be affected if the target firm occupied 20% of a concentrated market (leading firms). This test is designed to prevent large firms from becoming the dominant firms in concentrated markets where they have not participated previously.

It is generally believed that the effect of both tests would be to bar practically all contemplated mergers by firms meeting the very high threshold size requirements.

- <u>Senator Kennedy</u> would enact two tests:

  (1) Two firms each of which have revenues of more than $2.5 billion or assets of more than $2 billion would be barred from merging; and

  (2) Two firms each of which have more than $350 million in revenues or more than $200 million in assets must justify their merger by substantial economies of scale or other <u>efficiencies</u>.

  The goals are quite similar to those of the Justice Department's proposal however, both would lead to litigation over different questions.

- <u>The FTC</u> would not bar conglomerate mergers but would require acquiring firms above a given size to divest or "spin off" assets of equal size to those of the target firm. The Commission does not have a bill at this time but has proposed the spin off principle to those contemplating anti-conglomerate merger legislation as a moderate alternative to a total ban. We understand that Senator Kennedy may accept the provision.

Impacts of the Justice Proposal

CEA has reviewed the Department's proposal and, based on the bill's $2 billion in assets or sales rule, reached the following preliminary assessment of its impacts:

- o The largest 155 industrials, 12 transportation 20 life insurance companies, 36 general financial, and 22 retailers -- i.e., the largest 254 non-banking and non-utility companies -- will be prevented from acquiring any company with U.S. sales or assets over $100 million. This latter cut-off point probably extends to the 2,000th largest non-banking and non-utility company in the U.S. Thus, a large number of companies will be protected from possible "hostile" takeovers by the leading 254 companies.

- o Various combinations of the 196 companies (450 minus 254) and the third tier 1550 (2000 minus 450) will be prohibited. Again, a large number of possible "hostile" takeovers will be ruled out.

- o The leading 284 industrial firms (manufacturing and mining), 21 transportation, 47 life insurance, 50 general financial, and 48 retailing companies would effectively become immune to takeovers. I.e., the largest 450 non-banking and non-utility companies in the U.S. would be protected from "hostile" takeovers by any other U.S. company. The 20% market share prohibition will protect yet more companies.

Political Costs and Benefits

The arguments for supporting some limitation on conglomerate mergers are:

1. It is a tradition of the Democratic Party to seek to limit the power and influence of big business. Senator Kennedy will submit a bill and hold hearings and we may be criticized in traditional liberal

Democratic circles if we do not favor the concept. It will help your dealings and the Attorney General's (who favors this concept) dealings with Senator Kennedy, who now chairs the Judiciary Committee.

2. There is a fair amount of concern in the country generally about the wave of mergers. Ordinary citizens are likely to support the idea.

3. Labor is likely to be supportive.

4. In a year when we are perceived by many Democrats as having a budget which cuts against many traditional Democratic programs and constituencies, it would be helpful to be able to support a bill of this type.

5. Small business, through the National Federation of Independent Business, has expressed interest in supporting some legislation in this area.

Arguments against:

1. The economic evidence is at best neutral so that we are likely to be left with the "bigness is bad" justification.

2. The bill is not likely to pass this session. Beyond Kennedy, it is not at all clear that there is great interest or support elsewhere in the Senate or in the House.

3. Big business is predictably strongly opposed to the idea and the Business Roundtable has suggested that it will affect their willingness to be helpful in other areas. The Roundtable perceives an anti-merger bill as the most threatening item on the Administration's agenda. They argue that mergers perform a positive benefit in that they permit the merged firm to withstand cyclical negative trends, permits bilateral internal transfer of capital and often prevents business failures and their consequent disruptive effect. They believe that government should not interfere in the operation of the free market absent a demonstrable evil which they contend does not exist at the present time.

4. The legislation, as drafted, restricts takeovers based on the size of assets in the United States. This would ease takeovers by foreign and multi-national firms which are larger than the U.S. firms but which may not be barred under the bill.

Other considerations:

1. The timing pressures on the Administration to reach a decision stem from the Attorney General's request for a decision in time for a State of the Union announcement Commerce, Treasury and OMB are unanimously opposed to a rushed judgment on a matter of such magnitude and impact. (Their detailed comments are stated below.)

2. Congressman Rodino commissioned a study by experts of conglomerate mergers. The report is due in a few weeks and we would be benefited by the views.

Departments and Agencies Comments

Commerce, Treasury and OMB believe that (1) the Justice proposal contains thin economic, social and political arguments for a matter of such importance; and (2) the risks involved with a rushed decision are enormous when compared to the possible benefits stemming from a State of the Union announcement.

- Commerce: "The Administration should move with great caution on this subject. No case has been made for the Justice proposal, there is little or no economic literature on this subject, there has been no public debate which would lay the foundation for such a proposal, and the impact is totally speculative .... The proposal attacks bigness per se and unfairly shifts the burden of proof .... The dollar limits are arbitrary and no defense is presented as to why the caps chosen are preferred to a cap either a quarter of a billion dollars higher or lower.... Some of the recent mergers (which would have been blocked had the proposal been in effect) actually increased efficiency. It is misleading to conclude without analysis that the impact of each of them was adverse.... The proposal (1) may encourage foreign takeovers; (2) reduce competition and (3) adversely affect business confidence. One of the principal weaknesses of the proposal is that it views everything from the perspective of competition.... but there is no discussion of the underlying legal and economic conditions which influence corporate decision."

- Treasury: The Department expressed reservations about the Justice proposal and: (1) criticizes the lack of economic analysis; (2) states that it is not apparent from the Justice materials that concentration in the private sector has fallen since 1972; (3) points out that the proposal does not discuss the bias favoring foreign over U.S. firms. Treasury also recommends that if the Administration goes forward with the proposal that it be revised to: (1) include spin offs rather than ban conglomerate mergers; (2) justify any size limit rather than choose an arbitrary figure; and (3) articulate the basis for foreign firm treatment.

o OMB: Jim McIntyre recommends that you not approve the proposal. He recommends that you should go no further, at this time, than to announce a general expression of concern and a statement that you are directing Government officials to present you with suitable recommendations.

Conclusion and Recommendation

The Attorney General has asked that you support the bill and announce your support in the State of the Union. The major questions for you to address are whether anything be done in this area and if so, what.

The economic evidence in support of anti-conglomerate merger legislation is marginal. The departments and agencies have reviewed the Justice proposal under tighter time constraints than the subject warrants and we are in agreement that the bill should not be introduced on anti-competitive, anti-inflationary or economic grounds. Our view is that the traditional social and political grounds are the only plausible basis of support but that this provides a strong and adequate basis for support in a tight budget year. I believe the benefit you will get from consumer groups, Kennedy and liberals outweigh the downside from the business community.

Decision

________ Approve essentially the Justice Department bill, as a departmental priority, in cooperation with Congressional leaders, (DOJ, DOL, DPS, Wexler. The FTC also recommends approval if the spin off remedy is adopted.)

________ Disapprove proposal at this time. (Commerce Treasury)

✓ ________ No decision but further study until 2/15 (OMB, CEA prefer that you not decide the matter now, but if you choose to do so OMB recommends disapproval.)

J

Justice Department
Proposal

THE WHITE HOUSE
WASHINGTON

1/22/79

Attorney General Bell

The attached was returned in the President's outbox today and is forwarded to you for appropriate handling.

Rick Hutcheson

Office of the Attorney General
Washington, D.C. 20530

January 8, 1979

MEMORANDUM TO THE PRESIDENT

Re: Legislative Options on the Problem of Conglomerate Mergers

Our analysis of the conglomerate merger problem and our view of the Administration's options in the 96th Congress are set out on the following pages.

I believe that the conglomerate merger problem requires new legislation of the kind we are proposing, and that the proposal deserves mention in your State of the Union message.

If the proposal is so announced, the Administration can obtain support for a joint effort with key Congressional leaders for responsible legislation that addresses a problem of wide national concern.

I urge your approval of Option 2.

Respectfully,

Griffin B. Bell

Griffin B. Bell
Attorney General

Griffin - let me get agency review by 2/15 & then decide. This is new to me.
J

THE CONGLOMERATE MERGER PROBLEM: LEGISLATIVE OPTIONS

Large conglomerate mergers (i.e. the joining of firms producing different products) and the aggregation of economic power reflected by them continue to trouble responsible minds and will be the subject of legislative activity in the 96th Congress. They are widely perceived by the public as undesirable, based on the adverse social and political effects of increased aggregate concentration, and on concern over possible long-term economic effects as well. Most conglomerate mergers are beyond the reach of the present merger law.

The problem is now underscored by a resurgence of conglomerate merger activity. The number of mergers involving a purchase value of more than $100 million totalled 80 in 1978, compared to 41 in 1977, 39 in 1976, and 14 in 1975. During 1977, mergers by manufacturing and mining firms with assets of over $1 billion totalled 28 and involved total assets of $4.659 billion, compared with 18 such mergers in 1976 involving total assets of $2.530 billion. In the last decade, 1968-1977, industrial firms with more than $1 billion in assets acquired 160 enterprises in conglomerate mergers, with the acquired firms averaging $130 million in assets. In recent years, conglomerate mergers have represented 80 to 90 percent of merger activity by asset size, contrasted with only 38 percent in 1950.

Large conglomerate mergers are viewed as socially and politically undesirable because they concentrate power in the hands of the few corporate managers of the conglomerate empires, remove corporate headquarters or control from smaller cities to larger ones, and make companies more impersonal and less responsive to the specific needs of particular markets.

Aggregate concentration of economic power in our country, measured by a number of different yardsticks, has not diminished since World War II, but rather continues its long-term upward trend. Chart A, attached, depicts the trend toward increased aggregate concentration, as reflected by six different data series. Large conglomerate mergers clearly accentuate the problems of aggregate concentration; as Chart B illustrates, about 13 percent of the total assets of 1975's top 200 industrial companies represented assets acquired by mergers.

There is also considerable evidence that many large conglomerate mergers are not based on any expected efficiencies or synergism, but simply reflect the financial attractiveness of the transaction at a given stock or asset price, or the desire of management to use surplus funds to acquire existing companies rather than invest in new plant and equipment or distribute the funds to stockholders. Finally, while there is no consensus, many antitrust lawyers and economists continue to believe that large conglomerate mergers will produce long-run anticompetitive effects by lessening the number of firms that might become significant potential competitors to each other, creating diseconomies of scale, creating a mutual interdependence of firms that meet each other in many markets, and increasing the possible financial barriers to entering markets to compete against the participating firms. The difficulty is in proving such effects in individual markets, as is now required under current merger law.

In 1976, Congress evidenced continuing concern about mergers by enacting the pre-merger notification statute, affecting transactions in which firms with assets or sales of over $100 million acquire other firms with assets or sales of over $10 million. Notification to the Justice Department and Federal Trade Commission, however, does not change the substantive standards of Section 7 of the Clayton Act -- under which most conglomerate mergers cannot successfully be challenged.

In the 96th Congress, it is clear that both the Senate and House Judiciary Committees will consider new legislation directed at conglomerate mergers. (In the 95th Congress, Senator Kennedy held hearings and Chairman Rodino commissioned a study of conglomerate mergers). Senator Kennedy has made clear his intent to introduce legislation early in the 96th Congress (probably a total ban on all mergers over a certain size), but has also asked to work out a joint proposal with the Administration if an Administration bill is approved. Proposals will range from an outright, total ban on mergers among and by the "Fortune 500" or some portion of them, on the one extreme, to proposals for minor tinkering with the government's burden of proving anti-competitive effects in particular markets, on the other. Some, of course, will argue that no change should be made in the current law on the grounds that there is no definitive proof of specific harm from conglomerate mergers, that incumbent managements need the threat of takeovers to remain efficient, and that philosophically no restrictions should be placed on the flow of capital. The business community will likely be split on the issue (few businessmen like a "hostile" takeover).

The Department of Justice believes that the conglomerate merger problem requires new legislation, and proposes a "middle-ground" statute that it believes can achieve the support of Congressional leaders if backed early by the Administration as part of a joint effort.

The Justice Department's proposed statute would change the law's presumption so as to make proponents of a merger of very large firms prove that the preponderant effect of the merger will be to substantially enhance competition (rather than requiring the government to prove that the merger may substantially lessen competition). Two classes of transactions would be affected by the proposed statute: (1) large firms whose combined sales or assets would total $2 billion or more; and (2) any firm with $1 billion or more in assets or sales if it wishes to acquire a leading firm (20 percent or more of net sales) in a sizeable and concentrated relevant market (a market with $100 million or more of sales in which the four-firm concentration ratio exceeds 75 percent). To address the problem of foreign firms doing business in the United States, the statute would provide that a majority of the leading firm's assets must be located in the United States.

The basic theory of the Justice Department's proposal is to deter transactions of the defined classes <u>unless they have a positive effect on competition</u> and thus a positive effect in the long-run for consumers, and not continue to permit them for the short-term benefit of the companies involved, with no requirement for proof of socially and economically desirable results. In the broadest sense, the rationale is that our largest companies should be diverted from attempting to acquire one another and from attempting to acquire the leading firms in highly concentrated industries, thus potentially releasing their energies into more economically and socially desirable areas.

The proposal's effect can be seen using 1977 assets and sales data: unless the preponderant effect would be substantially to enhance competition, the 128 largest industrials (ranked by sales) could not acquire any firm with sales or assets of more than $100 million and the 242 largest industrials could not merge with larger firms. Similarly, the 40 largest retailers (in sales), the 47 largest diversified-financial companies (in assets), and the 45 largest life-insurance companies (in assets) could not merge with larger firms without proof of a positive effect on competition. Moreover, without such proof, none of these firms could acquire a leading firm in a sizeable concentrated market.

Chart C shows that over the past 30 years, the proposed statute's combined-asset provision (if it had been in effect) would have challenged only about 5% of the large merger transactions, but would have dealt with about 29% of the assets acquired in manufacturing and mining mergers. As shown on Chart D, during the years 1975-1977, the combined-asset provision would have affected 19 mergers, but would have dealt with 44.6% of the assets acquired in large mergers. In short, the statute has a responsibly narrow focus.

OPTIONS

The Administration's options in dealing with the conglomerate merger problem in the 96th Congress appear to be:

Approved ____

Option 1 -- Propose conglomerate merger legislation at the earliest moment, independently of others who have expressed interest in the issue.

Approved ____ Option 2 -- Propose essentially the Justice Department bill, if possible in cooperation with Congressional leaders, early in the 96th Congress.

Approved ____ Option 3 -- Propose an Administration conglomerate merger bill later in the 96th Congress.

Option 4 -- Decide now that the Administration will not initiate any conglomerate merger proposal, but will respond to the proposals of others by

Approved ____ (A) (A) opposing any new legislation

or or

Approved ____ (B) (B) allowing the Justice Department to respond favorably to the initiatives of others by advocating an approach similar to its draft bill.

The Department of Justice strongly urges that Option 2 be approved. Debate would be structured around a well-constructed proposal rather than some more extreme measure, and the Administration will share credit for the initiative in this matter. In the event a different option is to be chosen, the Department of Justice urges approval of Option 4(B), although the credit for the initiative would go to others.

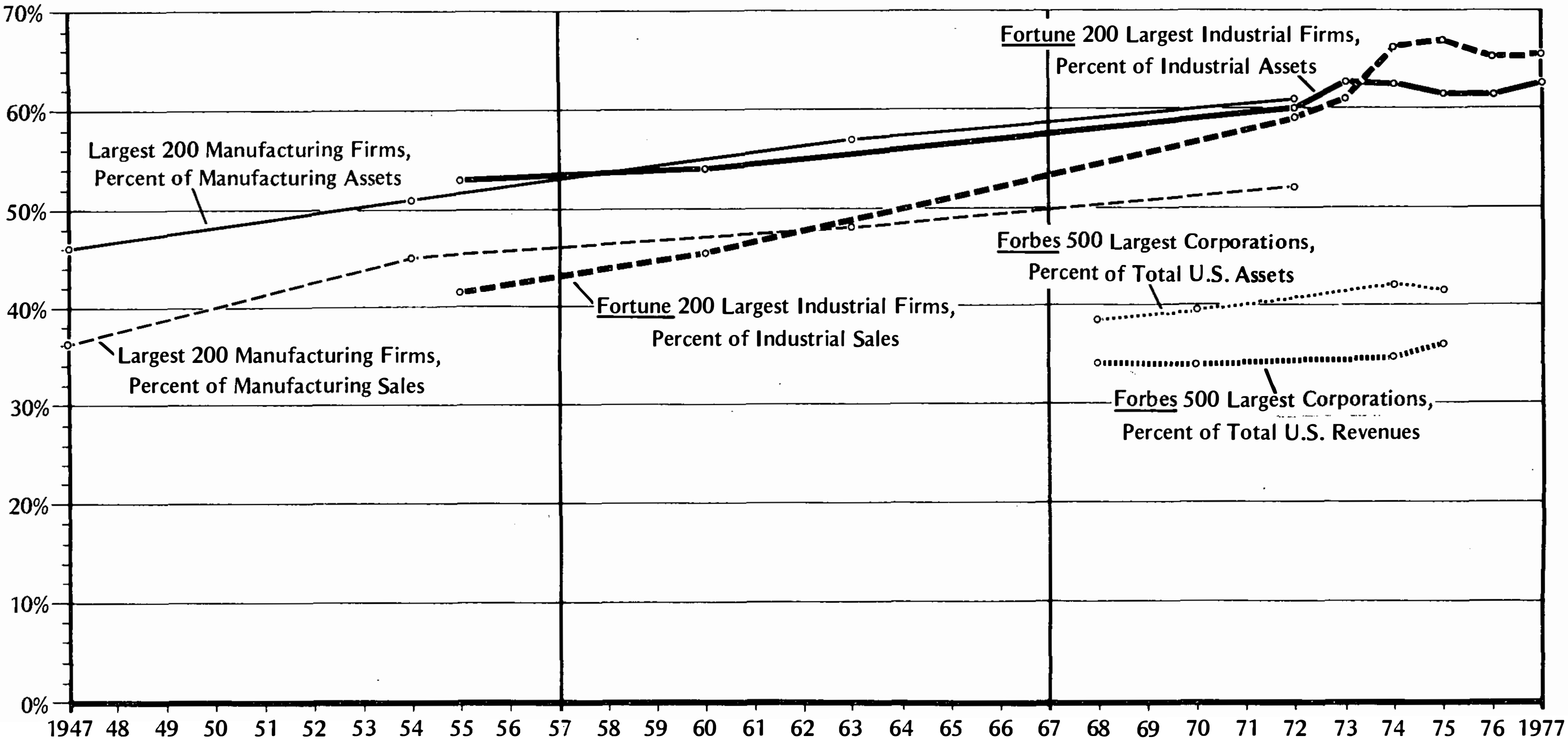
In our view, Option 1 is not realistic in view of the short time-frame remaining before the 96th Congress convenes, at which time those Congressional leaders who have previously taken a position on the issue will undoubtedly introduce their own bills.

Option 3 has little merit other than giving us time to accumulate more data which likely will not substantially alter the fundamental issues.

Finally, Option 4A would not only leave unaddressed the adverse effects of conglomerate mergers, but would place the Administration in opposition to those who believe that the harmful social and political effects should be corrected. It would be viewed as a retreat from the Administration's previous strong support for the pro-competitive effects of strong antitrust enforcement.

Attachments

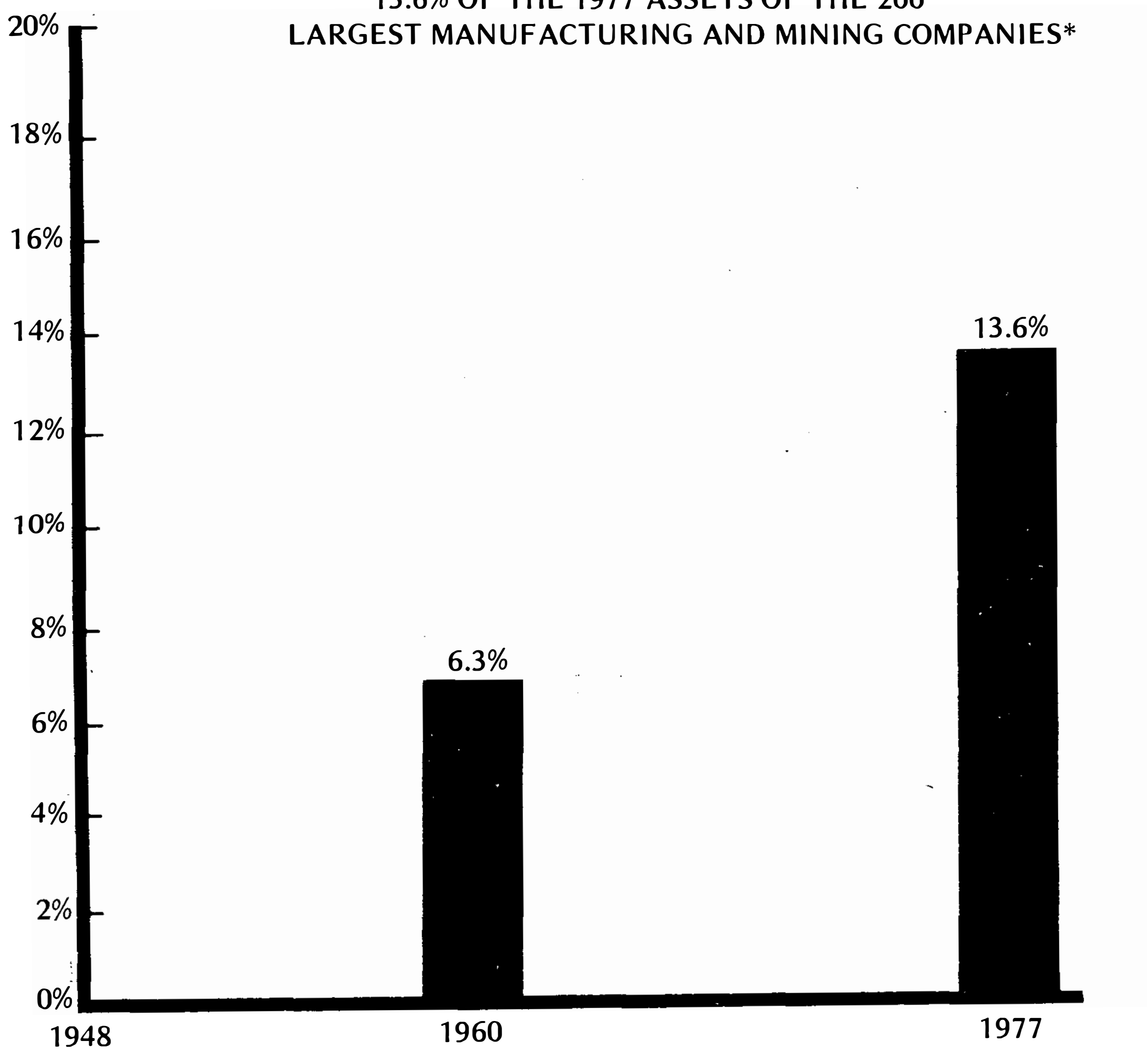
CHART A
TRENDS IN AGGREGATE CONCENTRATION, BY VARIOUS MEASURES



Source: Justice Department Tables Based on Data from Various Sources.

CHART B

ACQUISITIONS SINCE 1948 EQUALLED
13.6% OF THE 1977 ASSETS OF THE 200
LARGEST MANUFACTURING AND MINING COMPANIES*



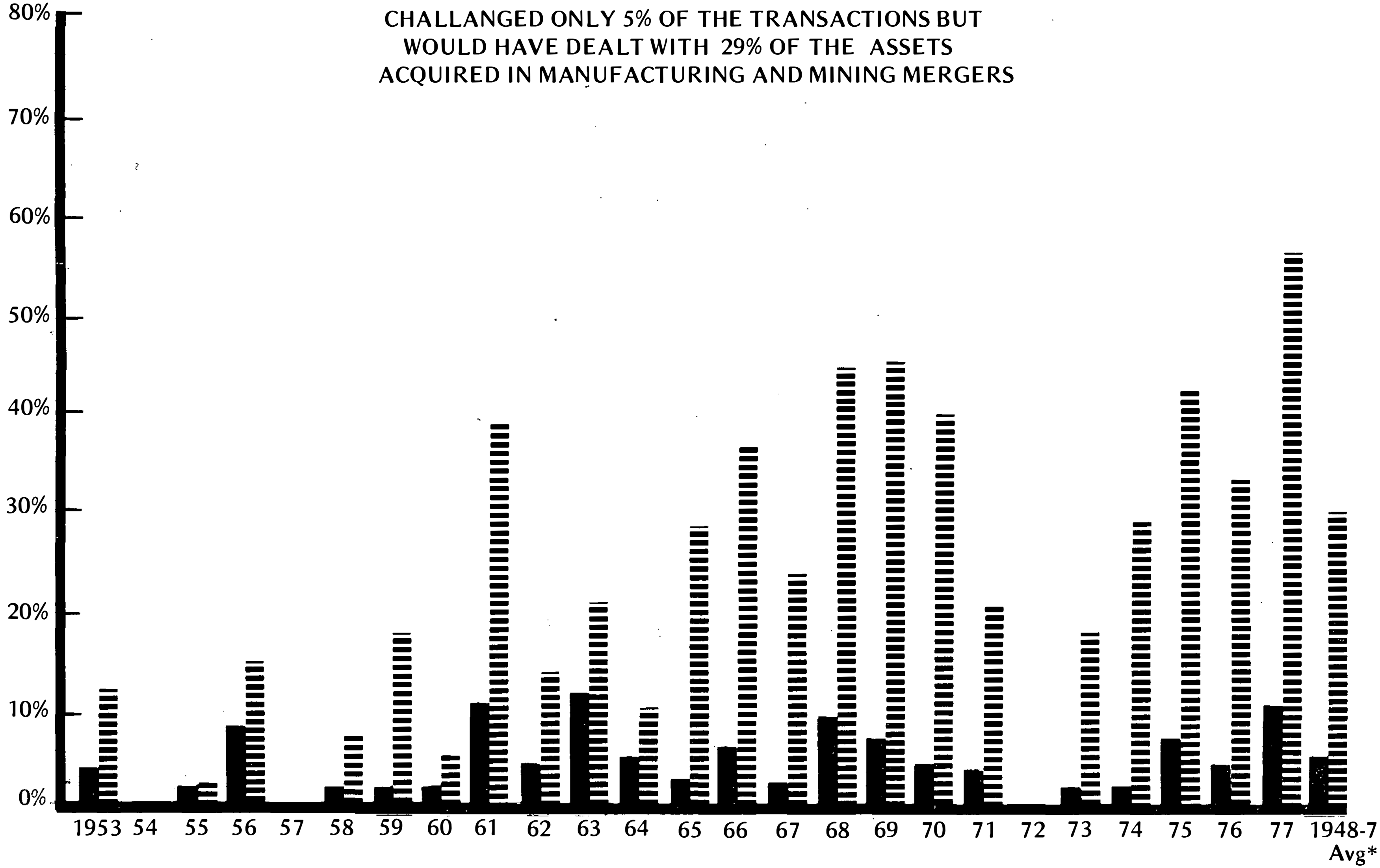
CUMULATIVE ASSETS ACQUIRED IN MERGERS, IN CONSTANT DOLLARS, AS A PERCENT OF ASSETS IN GIVEN YEAR.

*RANKED BY 1975 ASSETS.

SOURCE: JUSTICE DEPARTMENT COMPUTATIONS BASED ON DATA FROM VARIOUS SOURCES.

CHART C

OVER THE PAST 30 YEARS, THE COMBINED-ASSETS PROVISION OF THE PROPOSED LEGISLATION WOULD HAVE CHALLANGED ONLY 5% OF THE TRANSACTIONS BUT WOULD HAVE DEALT WITH 29% OF THE ASSETS ACQUIRED IN MANUFACTURING AND MINING MERGERS



PERCENT OF TRANSACTIONS CHALLENGEABLE

PERCENT OF ASSETS CHALLANGEABLE

*AVERAGE WEIGHTED ON BASIS OF CONSTANT 1977 DOLLARS. NO MERGERS WOULD HAVE BEEN COVERED IN 1948-52.

SOURCE: JUSTICE DEPARTMENT COMPUTATIONS BASED ON DATA FROM THE FEDERAL TRADE COMMISSION.

CHART D

Mergers Consummated in 1975-1977 Which Would Have Been Challengeable Under the Combined-Assets Provision of the Proposed Statute

Year	Acquiring Firm	Assets (millions)	Acquired Firm	Assets (millions)
1975	International Paper	2,729.9	General Crude Oil	108.4
	Esmark Inc.	1,473.9	International Playtex	182.0
	Gulf & Western	2,683.0	Kayser-Roth Corp.	402.0
	United Technologies	1,820.1	Otis Elevator	764.2
	Signal Companies	1,532.9	Universal Oil Products	443.1
1976	Gulf & Western	3,305.7	Marquette Company	155.4
	Marathon Oil Co.	2,005.4	Pan Ocean Oil Corp.	137.4
	Colgate-Palmolive	1,443.6	Riviana Foods Inc.	269.0
	General Electric Co.	9,763.5	Utah International Inc.	1,130.8
1977	Union Carbide	6,621.6	Amchem Products	97.4
	Atlantic Richfield	8,853.3	Anaconda Co.	2,050.9
	IT&T Corp.	11,070.1	Carbon Industries	105.3
	Kennecott Copper	2,308.8	Carborundum Co.	532.2
	Beatrice Foods	2,128.9	Harman Intl. Inds.	103.1
	Champion International	2,180.5	Hoerner-Waldorf	365.7
	Gulf Oil Corp.	13,449.0	Kewanee Industries	389.0
	Union Oil of Calif.	4,226.8	Molycorp Inc.	163.6
	Tenneco Inc.	7,177.1	Monroe Auto Equipment	190.3
	St. Regis Paper Co.	1,489.2	Southland Paper	296.6

Source: FTC Statistical Report on Mergers & Acquisitions

NOTE: Dollar limits of the statute are deflated from January 1, 1979 using the Consumer Price Index.

Treasury
Comment

THE SECRETARY OF THE TREASURY
WASHINGTON 20220

PRIORITY

January 18, 1979

MEMORANDUM FOR THE PRESIDENT

I wish to bring to your attention that the mere rumor that you may endorse the proposal on conglomerate mergers in the State of the Union is rapidly raising concern and disquiet in the business and financial community. This trend has accelerated greatly since Treasury's memorandum of January 12 opposing the idea on the merits.

It remains true that the proposition cannot be defended on any sensible economic grounds and is sustainable only as a statement of social policy, although the economic weaknesses severely undermine the validity of that approach.

The main point that you must now also consider, however, is the certainty that your endorsement will cause a major fight with the business and financial community. Their cooperation with this Administration will decline and the impact on the fight against inflation will be negative.

I strongly question whether it is wise politically for us to take that issue on at this particular time and to blur what ought to be the clear thrust of our economic policy: to bring inflation under control and to induce everyone to cooperate in this effort. I, therefore, want to urge more strongly than I did before that this not become a part of your State of the Union recommendations and would greatly appreciate a chance to talk with you about this if you are inclined to decide otherwise.

Mike

W. Michael Blumenthal

OMB Comment

THE WHITE HOUSE
WASHINGTON

1/22/79

Jim McIntyre

The attached was returned in the President's outbox today and is forwarded to you for your information.

Rick Hutcheson

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

JAN 15 1979

MEMORANDUM FOR THE PRESIDENT

FROM: James T. McIntyre, Jr. J

SUBJECT: Justice Department Proposal on Conglomerate Mergers

Neither OMB nor other Federal agencies have had sufficient time to analyze Justice's proposal to preclude mergers of very large firms unless the proponents can demonstrate that competition would be enhanced and its recommendation that its proposal be included in your State of the Union Message. Based on preliminary discussions with selected agencies, it appears that:

- The economic evidence as to the effect of conglomerate mergers on concentration and other negative effects is mixed and inconclusive. To the extent that the justification will be based on their social undesirability, the objectionable aspects are assumed but not defined or otherwise articulated.

- The specific proposal of the Justice Department raises numerous questions which will require extensive analysis. The possibility of alternative approaches is nowhere discussed.

- The business community, whose cooperation is vital if the anti-inflation program is to succeed, will perceive the proposal as indicative of a "big is bad" philosophy regardless of how it is presented. We have had no indication that their views have been solicited.

Accordingly, we recommend that you not approve the proposal. If political factors argue in favor of immediate Presidential action, we recommend that any public announcement be limited to a general expression of concern and a statement that you are directing Government officials to present you with suitable recommendations.

Among the potential problem areas identified in the short time allotted for review of Justice's proposal are the following:

- To what extent, if any, will the proposal harm the small business sector (the source of much technical innovation and creative marketing techniques) by forcing larger firms to alter their acquisition policies in favor of absorbing smaller firms?

- Investors may be motivated to invest in small firms with a view toward their growth and subsequent acquisition by larger corporations. If so, to what extent will investment in small companies be discouraged by placing restrictions on the disposition of assets as the small company grows?

- What is the effect, if any, of size on the ability of large domestic corporations to compete successfully with huge multinational corporations?

- Are the dollar figures which trigger a reversal of the burden of proof realistic (e.g., firms with a value or sales of $100 million)? At this figure, and depending on the industry, it is questionable whether many firms will have achieved economies of scale with respect to research and development, have access to public and private capital markets on favorable terms, or have demonstrated sustained growth. Preventing their merger with larger firms may be unduly harsh for firms of that size. At a minimum, the Justice Department should explain its rationale for all figures and explain more fully the type of showing that would meet the standard of "enhancing competition."

- The Justice Department notes that critics of its proposal will point to the absence of economic evidence that conglomerate mergers are harmful, that managers of target companies need the threat of takeover to remain efficient, and that there is no philosophic justification for restricting the flow of capital. The draft options paper we have gives no indication of how Justice plans to respond to these criticisms.

- Full-fledged mergers eliminate entities as separate, independent business units. However, the proposal applies to other forms of asset acquisition which may not have the same potential for socially undesirable consequences.

- As FTC staff has noted in a paper prepared for the Domestic Policy Staff, large corporate acquisitions can supply needed capital in a firm's early stages, can provide additional liquidity, and can revitalize inadequate management. Concerned with losing these benefits, FTC staff notes the existence of alternatives.

One approach suggested by the FTC staff would be to require certain large corporations wishing to make an acquisition to spin off or divest themselves of a viable business entity with assets of comparable value. This would prohibit major increases in corporate size through merger but would permit efficiency-enhancing transactions. Another approach might be to amend the Clayton Act to prohibit, in addition to mergers which "substantially lessen competition," mergers of companies over a certain size which cannot be shown to produce substantial, demonstrable economies or efficiencies not otherwise achievable. This would eliminate acquisition for its own sake and might eliminate "financing" as a justification since, in most cases, other forms of financing (e.g., joint ventures with other firms) would be available. Such an approach would be more flexible and would permit economic considerations to be given more weight.

We do not suggest that either alternative is superior to that of the Department of Justice, but that they, and others, ought to be examined so that you have a choice beyond Justice's single option.

We do not believe that the contention that Senator Kennedy plans to introduce more extreme legislation should impel you toward any hasty action. We are not aware of any groundswell in the Congress at this time and suspect that the Senator may be taking an extreme position in order to force the Administration to initiate a proposal of its own. We perceive no reason not to wait for the study commissioned by Chairman Rodino that will be published in a few weeks.

If acceptable to you, I will direct my staff to submit the Justice Department proposal to selected agencies for detailed examination with a response date of mid-February. Consultations outside the Executive Branch should be undertaken by the Justice Department, the Domestic Policy Staff, and other interested agencies. The results can be provided to the EPG for their review. Alternatively, you may wish to extend the life of the Antitrust Review Commission in order to permit it to examine this proposal and suggest alternatives. The ability of the Antitrust Division to secure the Commission's endorsement would serve as a useful indicator of its potential success on the Hill.

Decision

Submit Justice proposal to agencies for response by mid-February.

Agree ✓ ____________ Disagree ____________

J

ID 790714

THE WHITE HOUSE

WASHINGTON

DATE: 23 FEB 79

FOR ACTION: STU EIZENSTAT

JACK WATSON

PHIL WISE

JERRY RAFSHOON OK for Bell, not for Pres

ANNE WEXLER

FRAN VOORDE

INFO ONLY: THE VICE PRESIDENT

JIM MCINTYRE

FRANK MOORE (LES FRANCIS)

SUBJECT: ATTORNEY GENERAL MEMO RE LEGISLATIVE OPTIONS ON THE PROBLEM OF CONGLOMERATE MERGERS

+++

+ RESPONSE DUE TO RICK HUTCHESON STAFF SECRETARY (456-7052) +

+ BY: 1200 PM MONDAY 26 FEB 79 +

+++

ACTION REQUESTED: YOUR COMMENTS

STAFF RESPONSE: ( ) I CONCUR. (✓) NO COMMENT. ( ) HOLD.

PLEASE NOTE OTHER COMMENTS BELOW:

fran

ID 7901297 NATIONAL SECURITY COUNCIL

REFERRAL DATE: 01 MAR 79

MEMORANDUM FOR: Rick Hutcheson

DOCUMENT DESCRIPTION: TO: ZB

FROM: BELL, G

DATE: 21 FEB 79

KEYWORDS: ECONOMICS CONGRESSIONAL

SUBJ: LEGISLATIVE OPTIONS ON THE PROBLEM OF CONGLOMERATE MERGERS

REQUIRED ACTION: FOR YOUR INFORMATION

DUEDATE:

COMMENTS:

FOR CHRISTINE DODSON

STAFF SECRETARY

------------------------- FOR NSC USE ONLY ---------------------------------

FOR INFO F O V C

(ICAO X)

MEMORANDUM

THE WHITE HOUSE

WASHINGTON

March 1, 1979

MEMORANDUM FOR: STU EIZENSTAT

FROM: HENRY OWEN HO

SUBJECT: Conglomerate Merger Proposal

I can't comment on the domestic merits of the Justice Department proposal that would tighten merger laws and give Justice authority over "giant mergers," in particular those involving conglomerates.

I note however, that the proposal is contested strongly by Treasury and Commerce, who challenge its "big is bad" premise, and State, which sees several potential international disadvantages. It is my understanding that the proposal was drawn up with little reference to international considerations. It could have the affect of encouraging foreign acquisition of U.S. enterprises and U.S. acquisitions of foreign firms. It is also possible that the ability of U.S. firms to compete overseas could be hampered.

I wanted to draw your attention to these possible international consequences of the proposal as you prepare your recommendation to the President.

ID 786649

THE WHITE HOUSE

WASHINGTON

DATE: 22 JAN 79

FOR ACTION:

INFO ONLY: THE VICE PRESIDENT | HAMILTON JORDAN
BOB LIPSHUTZ | FRANK MOORE (LES FRANCIS)
JERRY RAFSHOON

SUBJECT: EIZENSTAT MEMO RE CONGLOMERATE MERGER LEGISLATION PROPOSED BY THE DEPARTMENT OF JUSTICE

++

+ RESPONSE DUE TO RICK HUTCHESON STAFF SECRETARY (456-7052) +

+ BY: +

++

ACTION REQUESTED: IF YOU WISH TO ADD COMMENTS, DO SO IMMEDIATELY

STAFF RESPONSE: ( ) I CONCUR. ( ) NO COMMENT. ( ) HOLD.

PLEASE NOTE OTHER COMMENTS BELOW:

THE WHITE HOUSE

WASHINGTON

January 21, 1979

MEMORANDUM FOR: THE PRESIDENT

FROM: STU EIZENSTAT Stu
BOB MALSON B.

SUBJECT: Conglomerate Merger Legislation Proposed by the Department of Justice

The Attorney General has submitted the attached legislative proposal to curb conglomerate mergers by the nation's largest corporations and asks that you (1) approve its introduction and (2) announce your support in the State of the Union message.

Horizontal mergers (between competitors) and vertical mergers (among suppliers, manufacturers and sellers in a linked production and marketing chain) which would retard competition can be dealt with under existing antitrust laws. Those laws, however, have been interpreted not to prevent conglomerate mergers -- that is, acquisition by one company of another in a totally unrelated market where competition data is unavailable and generally stated in subjective, predictive terms. Justice believes that conglomerate mergers may have, in some instances, anti-competitive effects; that mergers between very large corporations should be permitted only if they would promote competition; and that the burden of proof should be on the companies seeking to merge. Justice believes these new standards are necessary because conglomerate mergers lead or could lead to increasingly larger concentrations of economic power which are undesirable politically and socially.

Economic Considerations

Conglomerate mergers which may have an anti-competitive effect are presently unlawful under Section 7 of the Clayton Act. But it is virtually impossible to prove the anti-competitive effect of the merger of firms in unrelated markets unless there is strong evidence of potential competition; i.e., that one of the firms was a potential entrant into one or more of the other firm's markets.

The Justice Department believes that the trend towards aggregate concentration of wealth and power is clear and should be curtailed without regard to the Government's ability to prove anti-competitive effects. If, in the future, the anti-competitive effects of conglomerate mergers can be proven under current law, the economy would most likely already be under the control of a small number of corporate managers. Such vast economic power, if it is to exist at all, should rest in the hands of elected officials.

Critics of the proposal (1) dispute the theory; (2) argue that the proof is inconclusive whether conglomerate mergers have an effect on compeition; and (3) believe the data on aggregate concentration is very mixed -- increases and decreases abound in different segments of the economy and vary depending upon the time period. The major elements of the economic discussion are:

- <u>Competition</u>: Little evidence exists that conglomerate mergers have affected competition. There is agreement on this point between those who propose anti-conglomerate merger legislation (Justice, FTC and Kennedy) and opponents (CEA, OMB, Commerce and Treasury).

- <u>Aggregate Concentration:</u> Justice states that merger acquisitions since 1948 have involved cumulative assets of 13.6% of the 200 largest manufacturing and mining companies. (Only a portion of that percentage was due to conglomerate mergers.) Justice argues that overall concentration has had a continuing upward trend over the last 35 years. Treasury counters that mergers occur in waves (we are in the third merger wave of this century) and overall concentration in the entire economy has been declining since 1972. It would appear that any increase is marginal over time. The evidence is cloudy on whether conglomerate mergers have contributed substantially to an increase in concentration.

- <u>Diversion of Funds:</u> It is alleged that conglomerate mergers divert corporate funds from productive investment in their own industries to buying up firms in other industries. This assertion is unsupported by evidence and we do not know what alternative options management would choose if conglomerate mergers were banned.

- Market Allocation of Resources: Enactment of the proposal might remove some of the competitive discipline of financial markets (applicable to the affected mergers) from the economy without a finding of a market failure.

Social and Political Considerations

Given the neutrality of the economic evidence, the social impact must be considered as the principal basis for anti-merger legislation.

"Bigness is bad" is the euphemism generally used to describe the common perception that it is not in the national interest to have huge concentrations of wealth and power in the hands of few people. This perception has a long history in the Nation's politics and thought but its elements are difficult to quantify and measure and thus are beyond the scope of the generally accepted instruments used by economists, financial analysts and antitrust experts who tend to dominate the scholarship in the field. The concept, in the final analysis, is both social and political in nature and its elements are:

- The lawful ability to concentrate economic power will breed anti-democratic political pressures.

- The range within which private discretion by a few in the economic sphere control the welfare of all should be limited.

- The free market sector of the economy should not be allowed to develop under antitrust rules that are blind to all but economic concerns.

Here the proposed remedies are not aimed at all firms above a given size. Rather, the proposals under review are targeted at large firms which seek to become larger through a particular mechanism -- mergers. Internal growth would not be precluded.

Proposed Remedies

- The Justice Department would prohibit the merger of firms whose combined assets and sales exceed a stated size unless it could be proven that competition would be substantially enhanced. Two alternative tests are involved:

(1) All corporate mergers exceeding $2 billion in combined sales and assets would be affected. This test is aimed solely at the size of the new entity and is designed to block the largest mergers.

(2) Acquiring firms with $1 billion in combined sales and assets would be affected if the target firm occupied 20% of a concentrated market (leading firms). This test is designed to prevent large firms from becoming the dominant firms in concentrated markets where they have not participated previously.

It is generally believed that the effect of both tests would be to bar practically all contemplated mergers by firms meeting the very high threshold size requirements.

- <u>Senator Kennedy</u> would enact two tests:

  (1) Two firms each of which have revenues of more than $2.5 billion or assets of more than $2 billion would be barred from merging; and

  (2) Two firms each of which have more than $350 million in revenues or more than $200 million in assets must justify their merger by substantial economies of scale or other <u>efficiencies</u>.

  The goals are quite similar to those of the Justice Department's proposal however, both would lead to litigation over different questions.

- <u>The FTC</u> would not bar conglomerate mergers but would require acquiring firms above a given size to divest or "spin off" assets of equal size to those of the target firm. The Commission does not have a bill at this time but has proposed the spin off principle to those contemplating anti-conglomerate merger legislation as a moderate alternative to a total ban. We understand that Senator Kennedy may accept the provision.

Impacts of the Justice Proposal

CEA has reviewed the Department's proposal and, based on the bill's $2 billion in assets or sales rule, reached the following preliminary assessment of its impacts:

- The largest 155 industrials, 12 transportation 20 life insurance companies, 36 general financial, and 22 retailers -- i.e., the largest 254 non-banking and non-utility companies -- will be prevented from acquiring any company with U.S. sales or assets over $100 million. This latter cut-off point probably extends to the 2,000th largest non-banking and non-utility company in the U.S. Thus, a large number of companies will be protected from possible "hostile" takeovers by the leading 254 companies.

- Various combinations of the 196 companies (450 minus 254) and the third tier 1550 (2000 minus 450) will be prohibited. Again, a large number of possible "hostile" takeovers will be ruled out.

- The leading 284 industrial firms (manufacturing and mining), 21 transportation, 47 life insurance, 50 general financial, and 48 retailing companies would effectively become immune to takeovers. I.e., the largest 450 non-banking and non-utility companies in the U.S. would be protected from "hostile" takeovers by any other U.S. company. The 20% market share prohibition will protect yet more companies.

Political Costs and Benefits

The arguments for supporting some limitation on conglomerate mergers are:

1. It is a tradition of the Democratic Party to seek to limit the power and influence of big business. Senator Kennedy will submit a bill and hold hearings and we may be criticized in traditional liberal

Democratic circles if we do not favor the concept. It will help your dealings and the Attorney General's (who favors this concept) dealings with Senator Kennedy, who now chairs the Judiciary Committee.

2. There is a fair amount of concern in the country generally about the wave of mergers. Ordinary citizens are likely to support the idea.

3. Labor is likely to be supportive.

4. In a year when we are perceived by many Democrats as having a budget which cuts against many traditional Democratic programs and constituencies, it would be helpful to be able to support a bill of this type.

5. Small business, through the National Federation of Independent Business, has expressed interest in supporting some legislation in this area.

Arguments against:

1. The economic evidence is at best neutral so that we are likely to be left with the "bigness is bad" justification.

2. The bill is not likely to pass this session. Beyond Kennedy, it is not at all clear that there is great interest or support elsewhere in the Senate or in the House.

3. Big business is predictably strongly opposed to the idea and the Business Roundtable has suggested that it will affect their willingness to be helpful in other areas. The Roundtable perceives an anti-merger bill as the most threatening item on the Administration's agenda. They argue that mergers perform a positive benefit in that they permit the merged firm to withstand cyclical negative trends, permits bilateral internal transfer of capital and often prevents business failures and their consequent disruptive effect. They believe that government should not interfere in the operation of the free market absent a demonstrable evil which they contend does not exist at the present time.

4. The legislation, as drafted, restricts takeovers based on the size of assets in the United States. This would ease takeovers by foreign and multi-national firms which are larger than the U.S. firms but which may not be barred under the bill.

private sector has fallen since 1972; (3) points out that the proposal does not discuss the bias favoring foreign over U.S. firms. Treasury also recommends that if the Administration goes forward with the proposal that it be revised to: (1) include spin offs rather than ban conglomerate mergers; (2) justify any size limit rather than choose an arbitrary figure; and (3) articulate the basis for foreign firm treatment.

- OMB: Jim McIntyre recommends that you not approve the proposal. He recommends that you should go no further, at this time, than to announce a general expression of concern and a statement that you are directing Government officials to present you with suitable recommendations.

Conclusion and Recommendation

The Attorney General has asked that you support the bill and announce your support in the State of the Union. The major questions for you to address are whether anything be done in this area and if so, what.

The economic evidence in support of anti-conglomerate merger legislation is marginal. The departments and agencies have reviewed the Justice proposal under tighter time constraints than the subject warrants and we are in agreement that the bill should not be introduced on anti-competitive, anti-inflationary or economic grounds. Our view is that the traditional social and political grounds are the only plausible basis of support but that this provides a strong and adequate basis for support in a tight budget year. I believe the benefit you will get from consumer groups, Kennedy and liberals outweigh the downside from the business community.

Decision

_______ Approve essentially the Justice Department bill, as a departmental priority, in cooperation with Congressional leaders, (DOJ, DOL, DPS, Wexler. The FTC also recommends approval if the spin off remedy is adopted.)

_______ Disapprove proposal at this time. (Commerce Treasury)

_______ No decision but further study. (OMB, CEA prefer that you not decide the matter now, but if you choose to do so OMB recommends disapproval.)

ID 790714

THE WHITE HOUSE

WASHINGTON

DATE: 23 FEB 79

FOR ACTION: STU EIZENSTAT w/ stu

FRANK MOORE (LES FRANCIS)

ALFRED KAHN NC

BOB LIPSHUTZ ~~ZEN~~ - concur

JIM MCINTYRE - NC

Zbig Brzezinski - with comments attached

INFO ONLY: THE VICE PRESIDENT

ANNE WEXLER

JACK WATSON

CHARLIE SCHUTLZE

SUBJECT: ATTORNEY GENERAL MEMO RE LEGISLATIVE OPTIONS ON THE PROBLEM OF CONGLOMERATE MERGERS

+++

+ RESPONSE DUE TO RICK HUTCHESON STAFF SECRETARY (456-7052) +

+ BY: 1200 PM MONDAY 26 FEB 79 +

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ACTION REQUESTED: YOUR COMMENTS

STAFF RESPONSE: ( ) I CONCUR. ( ) NO COMMENT. ( ) HOLD.

PLEASE NOTE OTHER COMMENTS BELOW:

THE WHITE HOUSE
WASHINGTON

07 Mar79

Jim McIntyre

The attached was returned in the President's outbox today and is forwarded to you for appropriate handling.

Rick Hutcheson

Jack Watson

	FOR STAFFING
	FOR INFORMATION
	FROM PRESIDENT'S OUTBOX
	LOG IN/TO PRESIDENT TODAY
	IMMEDIATE TURNAROUND
	NO DEADLINE
	LAST DAY FOR ACTION

FOR ACTION	FYI	
		VICE PRESIDENT
		JORDAN
		EIZENSTAT
		KRAFT
		LIPSHUTZ
		MOORE
		POWELL
		RAFSHOON
		WATSON
		WEXLER
		BRZEZINSKI
		MCINTYRE
		SCHULTZE
		ADAMS
		ANDRUS
		BELL
		BERGLAND
		BLUMENTHAL
		BROWN
		CALIFANO
		HARRIS
		KREPS
		MARSHALL
		SCHLESINGER
		STRAUSS
		VANCE

		ARONSON
		BUTLER
		H. CARTER
		CLOUGH
		CRUIKSHANK
		FIRST LADY
		HARDEN
		HERNANDEZ
		HUTCHESON
		KAHN
		LINDER
		MARTIN
		MILLER
		MOE
		PETERSON
		PETTIGREW
		PRESS
		SANDERS
		WARREN
		WEDDINGTON
		WISE
		VOORDE

	ADMIN. CONFIDEN.
	CONFIDENTIAL
	SECRET
	EYES ONLY

EXECUTIVE OFFICE OF THE PRESIDENT

OFFICE OF MANAGEMENT AND BUDGET

WASHINGTON, D.C. 20503

March 6, 1979

ACTION

MEMORANDUM FOR: THE PRESIDENT

FROM: James T. McIntyre, Jr. Jim

SUBJECT: Supplemental Budget Requests

This memorandum suggests that you reemphasize that budget supplementals or amendments not be requested unless urgently needed under tight criteria.

DISCUSSION

In 1977, at your direction, I informed the agencies that budget supplementals and amendments should be requested only when they are essential under specific criteria. Now, when we must restrain Federal spending, I think that this policy should be reiterated. The Congress is almost certainly going to need to enact a Third Resolution for 1979 that will raise budget outlays above their current ceiling of $487.5 billion. Both OMB's and CBO's current estimate is around $494 billion. The Administration should avoid proposals that will raise still further the totals in the 1979 Budget Resolution as well as 1980 totals.

RECOMMENDATION

I propose to send the attached memorandum to agency heads. I also suggest that the memorandum be distributed to members of the Cabinet at an upcoming Cabinet meeting so that both you and I can make a direct and personal plea for restraint.

Approve ✓ Disapprove__________

J

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

MEMORANDUM TO HEADS OF EXECUTIVE DEPARTMENTS AND ESTABLISHMENTS

SUBJECT: Budget Supplementals and Amendments

In this time of high inflation, it is imperative that we exercise budget restraint. One important way to do this is for each of us to interpret strictly existing criteria for budget supplementals and amendments. The President has asked me to remind you of those criteria and the vital need to avoid requests that will increase the budget. Annual budget requests are expected to cover all anticipated needs, including continuation of existing programs that require new authorizing legislation.

You are reminded of existing requirements of OMB Circular No. A-11 that supplementals and amendments will be considered only when:

- existing law requires payments to be made within the fiscal year;
- liability accrues under the law and it is in the Government's interest to liquidate the liability as soon as possible;
- an emergency situation arises that requires unforeseen outlays for the preservation of life or property;
- increased workload is uncontrollable except by statutory change; or
- new legislation enacted after the submission of the annual budget will require additional funds within the fiscal year.

You are asked to make every effort to absorb additional costs, including those permitted by the above criteria, from existing funds. Consideration of absorption should include the possibility of offsetting essential increases in other appropriation accounts. Whenever possible, required requests will be transmitted with the regular budget. In any case where supplementals are determined to be urgently needed and necessary under the above criteria, your staff should consult with OMB on the need for the request and its timing.

Through a cooperative effort we can help the President achieve his objective of eliminating all requests that would increase the budget except those that are absolutely necessary.

James T. McIntyre, Jr.
Director

ID 790905

THE WHITE HOUSE

WASHINGTON

DATE: 07 MAR 79

FOR ACTION:

INFO ONLY: THE VICE PRESIDENT

STU EIZENSTAT

JERRY RAFSHOON

JACK WATSON

ANNE WEXLER

CHARLIE SCHULTZE

ALFRED KAHN

SUBJECT: MCINTYRE MEMO RE SUPPLEMENTAL BUDGET REQUESTS

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\+ RESPONSE DUE TO RICK HUTCHESON STAFF SECRETARY (456-7052) +

\+ BY: +

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ACTION REQUESTED: YOUR COMMENTS

STAFF RESPONSE: ( ) I CONCUR. ( ) NO COMMENT. ( ) HOLD.

PLEASE NOTE OTHER COMMENTS BELOW: