APPENDIX C

The Legal Environment for Industrial Policy

Legal constraints could preclude or limit the application of some kinds of policy measures directed at industrial competitiveness and economic efficiency in the United States, The possible constraints reflect not only constitutional principles, but also the traditional separation of Government and business enterprise in this country (ch. 8), The separation—more nearly an adversarial than a collaborative relationship—is deeply rooted in basic political attitudes, and has normally been perceived as healthy and desirable: it finds expression in the U.S. legal system.

The legal environment in the United States thus seeks, in many instances, to insulate Government from the private sector, both directly—as through Federal conflict of interest laws and numerous disclosure statutes, and indirectly—in antitrust and trade laws that embody fundamental presumptions against mercantilism and in favor of vigorous competition, Policy proposals of some types could raise legal issues because they would mandate precisely the behavior that the legal system presently attempts to limit or prevent,

Within the framework of the legal system, Government has, nevertheless, been granted increasing leeway to involve itself in the affairs of business and industry. The rapid growth of Federal regulation in the environmental, safety, health, and energy areas over the past 15 years is evidence of this trend. Government can certainly intercede in private trade and commerce-and in a substantial way. The basic question is: Would policy innovations be possible that could function effectively within the context of traditional Government-industry relations in the United States—as embodied in basic aspects of public law? Or, would industrial policy require new modes of interaction between the public and private sectors, and hence changes, perhaps fundamental, in that law?

A number of aspects of the legal environment for industrial policy are discussed in a general way below. The intent is to suggest topics of probable importance, the scope of industrial policy initiatives that have been suggested being too broad for examination in detail. Among these suggestions have been: tax incentives, including liberalization of business tax deductions and substantial tax cuts for individuals; creation of new Federal agencies: expansion of mechanisms for participation by business and labor in the activities of Government, including committees and commissions; development of programs for training, retraining, and assisting the mobility of labor; incentives for export-related manufacturing; import restraints such as surcharges and quotas: and formalized "economic planning"' [as in the Balanced Growth and Economic Planning Act of 1975).

Constitutional Issues

The U.S. Constitution imposes a variety of distinct restrictions on Government actions affecting private trade and commerce. Policies toward industry must conform with these—generally associated with the "Commerce Clause,'" delegations of congressional authority, State sovereignty, and equal opportunity.

Article I, section 8 of the Constitution—which contains the Commerce Clause—forms the basis for the Federal Government's broad powers to regulate private trade and commerce. The Constitution also ensures that Federal laws will have precedence over any inconsistent State and local laws. Over the years, the Supreme Court has continuously expanded the concept of interstate commerce: well-established guidelines now exist. The most fundamental of these allows Congress to exercise jurisdiction under the Commerce Clause whenever a commercial activity has a ' 'substantial economic effect" on interstate commerce.[1] Under this interpretation, even an activity taking place wholly inside one State may be within the scope of the Clause, so long as its effects extend to other States. For example, the Supreme Court has found the Commerce Clause broad enough to include the extension of Federal wage and hour protection to all workers in firms producing goods for interstate commerce.[2]

To the extent that industrial policies would apply to major economic sectors —those that produce goods or provide services that are integrally

[1]See, e.g., *Heart of Atlanta Motel Inc. v. United States*, 379 U.S. 241, 258-59 (1964).

[2]*Maryland* v. Wirtz, 392 U.S. 183 (1968).

part of the flow of interstate and foreign commerce—such policies should not be materially inhibited by the Commerce Clause, Suppliers and subcontractors to these industries would also be subject to Federal regulation to the extent that they form a significant part of chains of production and distribution of products or services that are part of interstate commerce.

Article I of the Constitution also contains language that has been interpreted as permitting Congress to delegate legislative authority—for example, the day-to-day work of implementing congressional law, But the permitted delegations of authority are limited, especially to private parties rather than to Government agencies, Such restrictions would apply to committees or commissions involved with industrial policy that included private citizens within their membership, Those whose business interests could be affected would find their participation especially circumscribed,

The 10th amendment to the Constitution contains the State sovereignty provisions, which limit the extent to which the Federal Government can infringe on activities integral to the sovereignty of the States—e.g., those essential to State and local government. To the extent that a court sees industrial policy as a response to a national emergency, it would be more likely to uphold actions that might otherwise be seen as infringements on State autonomy. The courts will typically employ a balancing test: the gravity of national problems found to exist by Congress will be taken into account as a factor to be weighed, along with the nature of the State interest at stake, the extent of the interference with that interest, and the duration of the restraint.

Incorporated into the 5th amendment due process guarantee is the 14th amendment equal protection provision. The protections extend to businesses as well as individuals, and could bar programs that favor one segment of industry over another without legitimate economic or social purpose, But before a court overturned Federal economic legislation on equal protection grounds, it would have to be persuaded that the legislation was clearly without justification.

Antitrust Laws

U.S. antitrust laws seek to preserve competitive markets by broadly proscribing many forms of coordinated or collaborative activities among business enterprises. As such, they embody a fundamental public policy against the rationalization of trade, as through private "orderly marketing agreements" or similar arrangements that would tend to reduce the independent character of decisionmaking by competing firms. Given the substantial and costly risks of antitrust liability (e.g., private treble damage actions) it seems clear that the antitrust laws could represent a substantial obstacle to at least some forms of possible policy initiatives seeking increased industry wide collaboration on commercial and trade matters.

In view of the basic free enterprise policies embodied in the antitrust laws, the courts have narrowly construed explicit congressional exemptions from their application, and have sharply limited the circumstances justifying implied exemptions, Further, even where Government regulation displaces the antitrust laws, the courts have indicated that agencies can abuse their discretion in failing to consider the impact of regulatory policies on competition.

From the standpoint of industrial policy, the most important antitrust provision is section 1 of the Sherman Act, prohibiting any agreement that is "in restraint of trade among the several States or with foreign nations,"[3] This section has been interpreted to prohibit all manner of agreements among competitors which fix or stabilize prices, allocate territories or customers, limit market entry, regulate production, use group boycotts, or similarly restrict competition among firms at the same level of trade. Programs involving joint ventures among competing firms, including joint R&D programs, pooling of technical or marketing information, or standard setting, would thus be subject to antitrust scrutiny.

The question of antitrust restriction on R&D has recently arisen in discussions of cooperative R&D on generic technologies in various industries, including semiconductors. In the 1960's, the Department of Justice brought a suit under the Sherman Act alleging unlawful restraint of competition in technological R&D in the automobile industry,[4] The automakers were accused of conspiring to slow the pace of technological developments aimed at meeting Federal exhaust emissions standards, Thus, joint venture and cooperative R&D programs, as well as pooling of tech-

[3] 15 U.S.C. sec. 1 (1976), Also relevant are the Sherman Act provisions, 15 U.S.C. sec. 2 (1976), which prohibit the monopolization of, or attempts or conspiracies to monopolize, "any part of the trade or commerce among the several States, or with foreign nations", and sec. 7 of the Clayton Act, 15 U.S.C. sec. 18 (1976), which prohibits corporate acquisitions of the stock or assets of other covered corporations "where in any line of commerce in any section of the country, the effect of such acquisition may be substantially to lessen any competition or tend to create a monopoly."

[4] *United States v. Motor Vehicles Manufacturers Association of the U.S.*, Inc., 1969 Trade Cases 91, par. 72,907 (C.D. Cal. 1969).

nical and marketing information, may continue to be challenged under antitrust provisions—by the Government or by private parties, The guidelines for joint R&D recently issued by the Department of Justice, discussed below, seem unlikely to have a dramatic effect on perceptions in this area,

The potential relevance of antitrust considerations for industrial policy was illustrated during 1980 in the context of Government plans to assist the domestic automobile industry, Secretary of Transportation Goldschmidt's task force considered a variety of steps that the Government might take—including trade, tax, credit, and unemployment assistance policies, One trade policy option would have been for the administration to urge voluntary restraints on automobile imports from Japan. However, this option was judged to run the risk of antitrust litigation as an informal trade restraint agreement.[5]

Antitrust statutes are among the more ambiguous in the United States. The Sherman Act is written in particularly general terms, and must frequently be interpreted by resort to the courts. Litigation is often prolonged and expensive; penalties can be high, including large sums in civil damages from private actions. Imprisonment may result from criminal antitrust actions. Some observers believe that uncertainties concerning antitrust enforcement, combined with such large risks, has a substantial inhibiting effect on the activities of business and industry. Others believe the activities inhibited to be primarily those that are clearly collusive and anticompetitive, and that present antitrust enforcement practices are necessary and effective.

Concerns of this type—related particularly to topics such as joint R&D or joint ventures for foreign trade—have recently received a good deal of attention. For example, in a message to Congress on October 31, 1979, President Carter emphasized the importance of stimulating industrial innovation, and acknowledged that antitrust laws have often been assumed to prohibit all cooperative R&D. He directed the Justice Department to issue a set of guidelines concerning antitrust implications of cooperative research;[6] these guidelines were published late in 1980, and seem a useful though limited step in removing ambiguity from this area of antitrust enforcement.[7]

In fact, much of the lore of antitrust is unpublished—although often enunciated in speeches by Government officials, copies of which are available from the Justice Department on request.[8] Under such conditions, the private sector is likely to be wary of any participation in industrial policy initiatives which may seem to carry risk of antitrust actions.

Antitrust enforcement also extends to international trade. For example, the voluntary restraint agreements (VRAs) on imports of steel—discussed in chapter 6—were challenged under the Sherman Act by Consumers Union,[9] As a result of the VRAS, nine Japanese steel companies, plus British Steel Corp., and a number of Western European steel firms belonging to the European Coal and Steel Community, jointly agreed to reduce the amounts of steel they would export to the United States. Consumers Union charged that the President and Secretary of State lacked the authority to negotiate these agreements, and also claimed that, even assuming such authority existed, VRAs were unlawful under section 1 of the Sherman Act.

As the case progressed in the district court, Consumers Union withdrew its Sherman Act claim, leaving a state of uncertainty that still exists surrounding such voluntary private agreements. Basically, the question concerns whether or not private agreements, negotiated or induced by the Government but falling short of outright governmental compulsion, enjoy some degree of protection from antitrust attack because of the Government's involvement. Also note that, although Consumers Union brought suit against the Government (specifically, the Secretary of State), private suits might have been filed in addition. Parties directly affected by the agreements—for example, purchasers of steel claiming that VRAs raised steel prices to artificially high levels—could have brought actions under U.S. antitrust laws against the foreign steel producers that were parties to VRAs (although this might have posed jurisdictional problems).

Trade Law

The executive branch has considerable discretion in negotiating trade agreements. Nonetheless, this discretion is limited in various ways—

[5]"Move Would Give Carter Free Hand," *Automotive News*, Aug. 11, 1980, p. 4.

[6]"Industrial Innovation Initiatives Remarks Announcing a Program to Encourage Innovation, and . . ." "Industrial Innovation Initiatives Message to the Congress Transmitting Proposed Initiatives," *Weekly Compilation of Presidential Documents*, Oct. 31, 1979, pp. 2070-2071.

[7]*Antitrust Guide Concerning Research Joint Ventures* (Washington, D.C.: Antitrust Division, Department of Justice, November 1980).

[8]For example, J. Davidow, "Unfair Competition in the U.S." (Brussels, Belgium: International Institute for the Study of Commercial Competition, May 5, 1980).

[9]*Consumers Union of U.S., Inc.* v. *Rogers*, 352 F. Supp. 1319 (D.D.C. 1973); *Consumers Union of U.S., Inc.* v. *Kissinger*, 506 F.2d 136 (D.C. Cir. 1974).

for example, by antitrust laws as indicated in the previous section. Other restrictions stem from international obligations the United States has assumed—e.g., under the General Agreement on Tariffs and Trade (GATT).

U.S. trade law includes a large body of treaties and executive agreements of both a bilateral and multilateral nature. Prior to 1947, American trade agreements were bilateral, However, since the appearance of GATT in 1947, most trade agreements entered into by the United States have been multilateral.[10]

The basic purpose of GATT was to create a freer environment for trade among the member nations and to discourage attempts by countries to promote their own industries or to create relative disadvantages for other nations' industries. GATT attempted to meet these objectives by developing a framework for eliminating tariff discrimination among member nations, by reducing barriers to free trade other than tariffs, and by moderating tariff levels, GATT provisions represent important limitations on the kinds of policies the United States as a member nation may adopt—whether to promote domestic industries in foreign trade or to protect domestic industries against foreign competition.

However, the legal status of GATT in the United States has been unclear since its signing. GATT has never been submitted to the Senate for its "advice and consent" pursuant to article II of the Constitution. Therefore it has never been ratified as a treaty. Indeed, language in trade legislation enacted by Congress in the decade following the signing of GATT expressly withheld congressional approval or disapproval.[11]

In April of 1979, the President's Special Trade Representative initialed the Multilateral Trade Agreements (MTAs) resulting from the Tokyo Round negotiations held under GATT. Several months later, Congress passed the 1979 Trade Act and officially approved and implemented the Agreements. Thus, the binding effect on the United States of at least the MTAs is clear—in the absence of judicial challenges to the unusual procedure of adopting separate implementing legislation to effectuate trade agreements entered into by the executive.

Major U.S. trading partners are parties to GATT and the MTAs. Accordingly, actions by the United States to assist domestic industries that are inconsistent with obligations under the Agreements—or are perceived by other signatories to be inconsistent—may be subject to diplomatic challenge under GATT.[12] Moreover, since the trading partners of the United States have generally similar trade laws, violation of MTA or GATT provisions by the United States could provoke retaliation by these countries, including the implementation of both tariff and nontariff measures to restrict U.S. exports.

While the MTAs limit the policies of member governments that could act as export subsidies, they do provide leeway in such policies, Governments may promote the health and vigor of their industries in a general manner, even though such policies have an indirect impact on foreign trade. Thus, GATT does not prohibit policies aimed primarily at domestic operations, and should not pose an obstacle to industrial policies with domestic goals.[13] Nonetheless, the issue of when domestic subsidies begin to interfere with international trade flows has often been a matter of contention within GATT, Considerable effort went into negotiating the subsidy code in the new Agreements to try to arrive at more workable procedures,

Freedom of Information Act; Government in the Sunshine Act; Federal Advisory Committee Act

The Freedom of Information Act (FOIA) lays down comprehensive requirements for the disclosure of records kept by Government agencies.[14] It makes disclosure of such information the rule, and provides the public with powerful procedural tools for enforcement. Although the FOIA embodies a basic public policy favoring open Government and public disclosure, the Act itself recognizes through a series of exemptions that not all of the Government business can be conducted in a fish bowl, Exceptions include national security matters, law enforcement investigations, and confidential business information, including trade secrets.

The breadth of FOIA'S applicability suggests that it could well apply to special Government

[10] General Agreement on Tariffs and Trade, 55 U.N.T.S. 194, T.I.A.S. No. 1700 (1947). There have been seven rounds of trade negotiations under the auspices of GATT since 1947, the most recent of which was the Tokyo Round (1975-79).

[11] See, e.g., 19 U.S.C. sec. 1351(a)(1)(A) (1976).

[12] Of course, GATT's restrictions applicable to the United States are also applicable to the activities of U.S. trading partners. Thus, actions by other signatories to GATT or MTAs which violate their obligations under the Agreements may be challenged by the United States.

[13] In the Goldschmidt automobile options analysis referred to above, a number of internal subsidies were considered for the domestic automobile industry.

[14] 5 U.S.C. sec. 552 (1976).

boards or corporations established for purposes of industrial policy. Thus, the scope and legal effect of the so-called "trade secrets" exception to FOIA are matters of potential importance. For example, some policy measures might call for significant submissions or exchanges of sensitive technological, commercial, or financial data—e.g., costs of production—the public disclosure of which could prejudice not only the firms involved, but also the achievement of the policy goals. [Financial harm is a basic test applied to FOIA exemptions.) The key question would appear to be whether the exceptions, as presently embodied in the Act, would he viewed by the private sector as adequate protection against the disclosure of confidential information. If not, private firms would be unlikely to cooperate in the policy.

What FOIA did for agency records, the Government in the Sunshine Act does for agency meetings. Enacted in 1976, the statute requires that ". ., every portion of every meeting of an agency shall be open to public observation."[15] The Chrysler Corporation Loan Guarantee Board, among other Government bodies, has complied with the Sunshine Law'.[16] The Sunshine Act does allow an agency to close its meetings under some circumstances, including all of the situations covered by FOIA exemptions—e.g., discussions of financial data, internal personnel rules, private personal records, and information on financial institutions.

The Federal Advisory Committee Act applies FOIA and Sunshine Act principles to advisory committees. It requires that "each advisory committee meeting shall be open to the public."[17] It also requires that: 1) notice of meetings be published in the Federal Register; 2) interested persons be permitted to "attend, appear before, or file statements subject to reasonable regulations;" 3) minutes and other records be kept and be made available to the public.

The Sunshine Act and the Federal Advisory Committee Act raise issues similar to those of FOIA—i.e., the willingness of individuals and firms in the private sector to participate in policy initiatives that might involve disclosures of confidential information.

Conflict of Interest and Financial Disclosure

Federal conflict of interest laws and regulations, as well as financial disclosure laws, could affect the formulation and/or implementation of policies that depend on recruitment of private citizens to work for the Government. These laws and regulations extend to part-time as well as full-time employment, and also to unpaid consultants. With some exceptions, they prohibit Government employees from having financial interests in Government activities: restrict the professional activities of former Government employees in terms of who they may represent before the Government as "agent or attorney"; prohibit Government employees from receiving compensation from nongovernmental sources: and prohibit Government employees from representing a client in a proceeding to which the United States is a party or has a direct or substantial interest.

The basic conflict of interest rule prohibits executive branch employees from participating in proceedings in which they have a financial interest.[18] The prohibition includes consultation and advising, as well as decisionmaking. Financial interest is broadly construed to refer to interests of family and associates.

A detailed Executive order has been issued implementing the conflict of interest statutes, and two Government agencies-the Office of Personnel Management and the Office of Government Ethics—oversee the operation of the statutes. In addition to these laws and regulations, under the Ethics in Government Act of 1978 many categories of Government employees must disclose detailed personal financial information.

These laws could pose obstacles to the implementation of some kinds of policies because individuals in the private sector with special expertise might either be disqualified outright or might find the prohibitions and restrictions onerous and disruptive of their careers outside Government. There are also potential conflicts of interest when Government officials with regulatory responsibilities over industry become members of special boards, committees, or task forces relating to that same industry.

[15] 5 U.S.C. sec. 552b (1976).
[16] See, e.g., 45 *Fed. Reg.* 47565 (1980)
[17] 5 U.S.C. app. 1 sec. 10(a)(1) (1976).

[18] 18 U.S.C. sec. 208

Government Ownership of Patents and Technology

If an industrial policy initiative were to involve Government stimulation or funding of R&D and innovation, questions could arise about the interest of the Government as opposed to the private sector in any resulting inventions or other proprietary technology. Furthermore, legal restrictions on the utilization of Government-owned technology by private firms might impede the commercial development of that technology.

A number of complex and conflicting policy considerations exist in this area. First, when public funds are used to generate new technology, it seems clear that such technology should be utilized for the benefit of the public. Moreover, where the technology represents a significant advance in the state of the art, and has competitive significance, it is also clear that affording exclusive use of the technology to one firm might detract from competition in the industry. This consideration is particularly important where the technological development supported by Government would not have been commercially feasible for any one firm acting alone. On the other hand, in the absence of exclusive licensing rights, private firms might not commercialize the new technology.

Current rules governing the licensing of technology generated either by Government employees or through Government funding reflect—but do not resolve—these competing policy considerations. Thus, there is a strong general presumption favoring nonexclusive licensing. And, while provision is ostensibly made for exclusive licensing where necessary to ensure commercial development, the Government in many cases still retains the right to require sublicensing and otherwise to assure broad dissemination of the technology in a manner potentially inconsistent with a grant of exclusive rights.

At present, different Government agencies—the Department of Energy, the National Aeronautics and Space Administration, the Department of Defense, the Environmental Protection Agency—have different rules governing the ownership and licensing of rights to inventions or discoveries they have supported financially. Sometimes these rules are developed by the agency itself, other times they are statutory. Thus, the rights of the Government and of private firms are not set out in a unified body of law. Each agency operates under its own distinctions, its own rules or statutes, and its own procedures. This lack of consistency has been widely perceived as undesirable—and a potential inhibition to innovation and the commercialization of new technologies. Several bills recently introduced before Congress have sought to remedy this situation.

Legal Challenges and Judicial Review

New policy initiatives toward industry might involve new statutes, amendment or repeal of existing statutes, promulgation or amendment of executive orders or agency regulations, or combinations of these. Moreover, depending on their substance and reach, implementation might be assigned to the executive branch, existing executive or independent agencies, Government corporations, new regulatory bodies, or combinations of such entities. In turn, actions taken might include informal policy statements or guidelines, rules of general and binding applicability to individuals or businesses, or specific enforcement actions to restrain conduct inconsistent with rules and statutes. At almost any step, affected or aggrieved parties might challenge such policy initiatives in the courts. Measures intended as components of industrial policy could be subject to delaying actions as well as the threat of being struck down.

Historically, when Congress has enacted regulations significantly affecting private economic interests, it has generally provided avenues for aggrieved persons to seek judicial review. If precedent is a guide, therefore, significant aspects of new policies would likewise be subjected to judicial scrutiny. Moreover, even where Congress does not expressly provide for judicial review of an agency's action—and assuming that it does not by statute expressly preclude judicial review—such review will generally be available under the Administrative Procedure Act, ’g which embodies a strong presumption in favor of judicial review of agency conduct.

Permeating the body of statutory and decisional law governing the activities of administrative agencies—as well as court review of these activities—are the often conflicting goals of: 1) efficient and effective administration and implementation by Government officials of congressional objectives; and 2) the protection of private property rights from unjust or excessive governmental interference—e. g., ensuring adherence by

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5 U.S.C. sec. 500 et seq., sec. 701 et seq. (1976)

the Government to constitutional and statutory guidelines.

Reflecting the great increase in Government regulation over the past 15 years, the entire area of administrative law is currently in a state of flux. Thus, while judicial challenges to new policies affecting industry might be frequent, it is difficult to do more than speculate on outcomes. However, under ordinary circumstances, the courts would probably not interfere at the preliminary stages of policy formulation. Once implementation commenced, depending on the interests affected by the policies in question, judicial challenges, including preenforcement challenges, could be expected. Whether preenforcement challenges would be entertained, and precisely at what point the courts would find that an agency's actions were "ripe" for judicial review, would depend on the availability of other means of judicial review, and the hardship of pursuing such means. In any event, it appears likely that at least some industrial policy initiatives representing substantial change from past practices would be challenged in the courts. At the least, such challenges might delay the implementation of new policy initiatives.