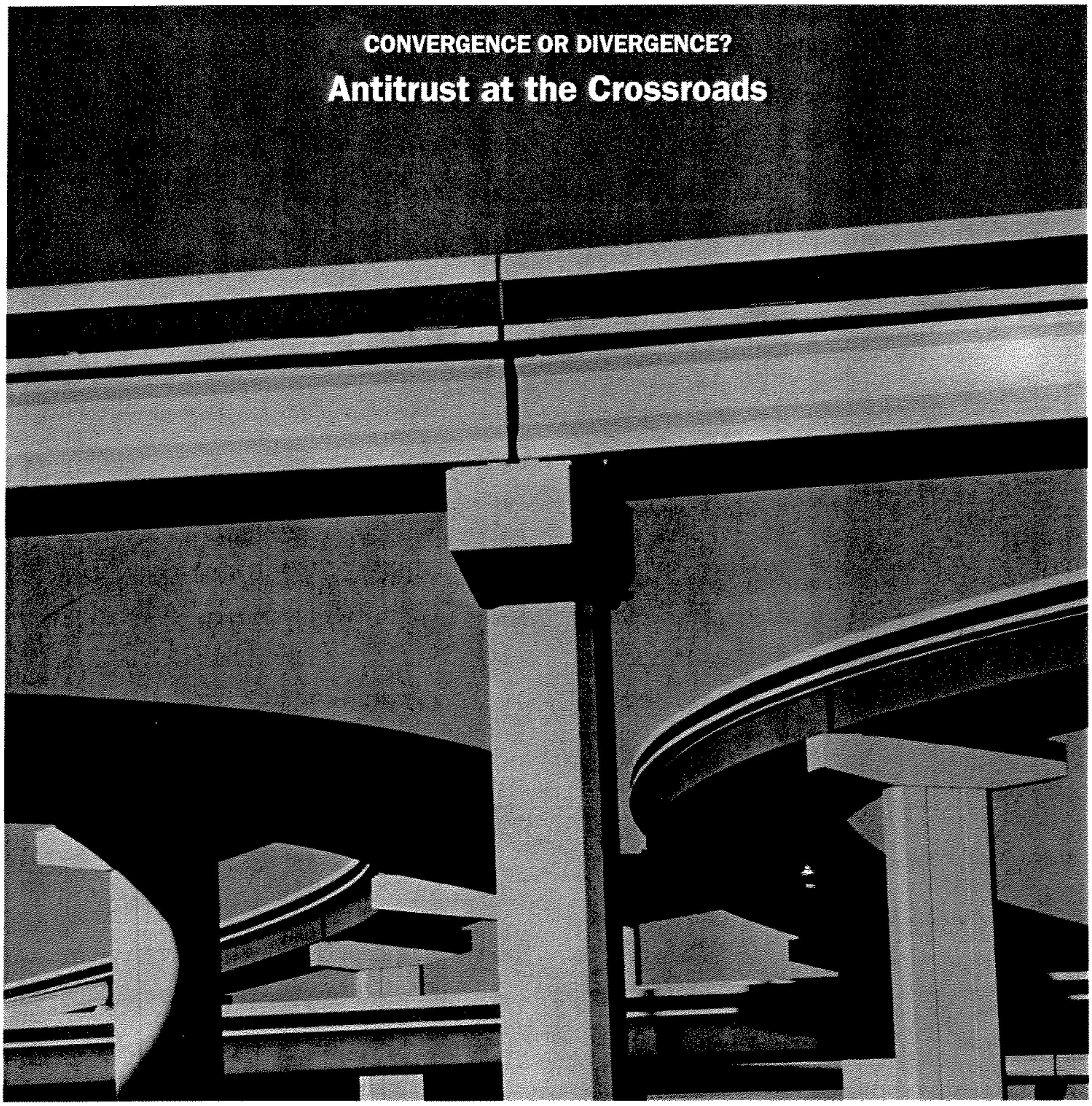
FALL 2001 · Volume 16 · Number 1

# ANTITRUST



DEVELOPMENTS

LESSONS FROM *BABY FOOD*:

# The Role of Efficiencies in Merger Review

BY WILLIAM J. KOLASKY

IN 1968, HARD ON THE HEELS OF THE U.S. Supreme Court's 1967 decision condemning Proctor & Gamble's acquisition of Clorox in part because the merger had made Clorox more efficient by lowering its advertising costs,[1] Oliver Williamson published his path-breaking article, *Economies as an Antitrust Defense: The Welfare Tradeoffs*.[2] Using a simple diagram that he called, with typical humility, his "naive model," Williamson taught us that where a merger both creates market power and produces significant efficiencies, the resulting tradeoff between the loss of allocative efficiency and the gain in productive efficiency generally favors permitting the merger to go forward. Williamson argued, therefore, that taking efficiencies into account in merger review was absolutely essential: "if neither the courts nor the enforcement agencies are sensitive to these considerations, the system fails to meet a basic test of economic rationality. And without this the whole enforcement system lacks defensible standards and becomes suspect."[3]

It took nearly fifteen years for enforcement agencies in the United States, with the issuance of Bill Baxter's 1982 Merger Guidelines, to agree formally to take efficiencies into consideration in reviewing mergers.[4] It took another eight years before any U.S. court accepted that efficiencies might be a defense to an otherwise anticompetitive merger.[5] As a result, more than thirty years after Williamson's watershed article, even the U.S. courts and enforcement agencies are still at the early stages of learning how to integrate efficiencies into merger analysis.

The best illustration is the recent decision by the United States Court of Appeals for the District of Columbia Circuit in *Federal Trade Commission v. H.J. Heinz Co.*,[6] reversing a district court denial of a Federal Trade Commission motion for a preliminary injunction to block the proposed merger of Heinz and Milnot Holding Company, the producers of two of the three leading brands of baby food, Heinz and Beech-Nut.[7] The district court, in a decision by Judge James Robertson, denied the injunction on the ground that the parties had successfully rebutted the structural presumption of illegality by showing that the merger was likely to produce substantial efficiencies that would enable Heinz and Beech-Nut, the number two and three brands, to compete more effectively against the dominant brand, Gerber, thereby leading to lower prices and better products for consumers. The court of appeals, in reversing, engaged in an extraordinary amount of appellate factfinding to find that the district court had given too much credence to the parties' claimed efficiencies and too little weight to the loss of competition between Heinz and Beech-Nut at the wholesale level.

This decision is worth studying because it illustrates the difficulties parties face in persuading courts and agencies that efficiencies are substantial enough to rebut the inference of anticompetitive effect that arises from *Philadelphia National Bank*.[8]

*William J. Kolasky is Deputy Assistant Attorney General for International Affairs in the Antitrust Division of the U.S. Department of Justice. He wrote this article prior to joining the Division. While in private practice, Mr. Kolasky co-signed, pro bono publico, a brief filed by Robert Bork on behalf of Citizens for a Sound Economy urging that the district court's decision in FTC v. Heinz be affirmed.*

## Background

To advocates for integrating efficiencies into the competitive effects analysis, the Heinz/Beech-Nut merger appeared to be a nearly ideal test case. The prepared baby food market in the United States had been dominated for more than a generation by Gerber, which had maintained a market share of between 65 and 70 percent for over thirty years. Heinz and Beech-Nut each had market shares of 15–20 percent nationally, but were almost never found on the same supermarket shelf and only rarely even in the same metropolitan area. Despite its position as the largest baby food maker in the world and despite having built a new, highly efficient, state-of-the-art manufacturing plant in the early 1990s, Heinz had never been able to overcome the strong brand loyalty enjoyed by Gerber and Beech-Nut, both of which had been in the U.S. market much longer than Heinz. Beech-Nut, on the other hand, suffered from having changed ownership multiple times and was now saddled with an old, inefficient plant. Faced with declining demand for prepared baby food, Beech-Nut could not justify the investment necessary to replace its obsolete facility. With Heinz's efficient new facility running at only 40 percent of capacity, the parties saw an opportunity for very substantial cost savings by moving Beech-Nut production to Heinz's more efficient plant, enabling them to combine Beech-Nut's strong brand equity with Heinz's lower production costs to compete more effectively against Gerber by offering consumers improved products at lower prices.

## The District Court Decision

The Federal Trade Commission staff, after several months of investigation, recommended against bringing a challenge.[9] The five commissioners split nearly evenly, voting 3–2 to bring the case.[10] The district court, after a five-day hearing in which it heard testimony from eight industry witnesses, two economists, and an accountant, denied the FTC's motion for a preliminary injunction.[11]

The district court found that the FTC had failed to show the requisite likelihood of success on the merits, given that both sides had stipulated that granting the preliminary injunction would effectively kill the merger.[12] In so ruling, the court applied the standard *Philadelphia National Bank* analytical framework.[13] The court held, first, that the relevant product market was prepared baby food and the relevant geographic market was the United States as a whole. The court held, second, that the FTC had established a prima facie case by showing that this market was highly concentrated, with the top three firms accounting for more than 90 percent of sales, and that the merger would substantially increase concentration by reducing these three firms to two. The court found, however, that Heinz and Beech-Nut had successfully rebutted the *PNB* presumption by showing that the merger would allow them to capture substantial efficiencies, which would enable them to compete more effectively against Gerber, and that the intensified competition between the merged firm and Gerber would benefit consumers far more than the relatively limited premerger competition between Heinz and Beech-Nut that would be lost as a result of the merger.

Because Heinz and Beech-Nut did not compete at retail, the court found that any elimination of competition between them at the wholesale level would have no adverse effect on prices to consumers. In making this finding, the court relied on evidence showing that the two brands were almost never found in the same supermarket and that they did not price against each other or even consistently monitor each other's prices. The court also relied on two econometric studies by the defendants' expert economist, Jonathan Baker, the former head of the FTC's Bureau of Economics. The first study showed that consumer substitution between the two brands was very small and that cross-elasticity of demand between them was not statistically significant. The second study found no discernible difference in the price of baby food whether there were two or three brands in the same metropolitan area.

At the wholesale level, the district court found that while there was direct competition between Heinz and Beech-Nut to be the second brand on the retail shelf, this competition typically took the form of fixed payments such as slotting fees, pay-to-stay arrangements, and new store allowances. The court found, based on a third econometric study by Professor Baker, that this past wholesale competition had no effect on the retail price of baby food. The court also found that the record left "substantial doubt" the merger would change the need for variable trade spending (such as merchandising funds to support temporary price reductions and sales) because Heinz and Beech-Nut both usually directed that variable trade spending at Gerber, not at each other.

Having found that the elimination of Beech-Nut as an independent competitor was unlikely to harm consumers, the district court went on to find that the efficiencies the parties claimed were merger-specific, substantial, and likely to benefit consumers. The court accepted Heinz's computation that it would realize between $9.4 and $12 million in merger-specific manufacturing cost savings by consolidating production of both brands in Heinz's modern, highly-automated Pittsburgh plant, which had sufficient capacity to handle the combined volume and still have 20 percent excess capacity for future increases in productions. The court credited testimony by Heinz executives that they expected also to realize substantial reductions in distribution costs by using Heinz's six distribution centers to distribute both brands and closing Beech-Nut's two redundant centers. The court found that Heinz would realize further savings by standardizing on the best recipes from each brand for each type of baby food. Finally, the court credited Heinz's testimony that the merger would facilitate greater innovation by giving Heinz sufficient presence on supermarket shelves to support the advertising needed to launch new products.

### The Court of Appeals Decision

In reversing, the court of appeals stepped well outside the usual role of an appellate court and engaged in a remarkable degree of appellate fact-finding. Its disagreement with the district court centered not so much on the applicable law, including the validity of an efficiencies defense to an otherwise anticompetitive merger, but rather on the district court's findings of fact, many of which it labeled clearly erroneous.

***Unilateral Competitive Effects.*** Focusing first on the district court's finding that the loss of competition between Heinz and Beech-Nut was of little importance because they were rarely found on the same supermarket shelf, the court of appeals held this finding clearly erroneous for three reasons. In each case, however, the court of appeals' reasoning seems more suspect than the district court's finding.

First, the court of appeals criticized the district court for failing to address record evidence showing that the two companies priced against each other and that where they were found in the same area prices were lower than where they were not.[14] In reaching this conclusion, the court of appeals simply ignored Baker's econometric studies, which the district court had credited and which showed no discernible difference in prices where Beech-Nut and Heinz were both present from where they were not. The district court found that study more persuasive than the anecdotal testimony and handful of company documents the FTC introduced to rebut it and on which the court of appeals relied.[15] Yet the court of appeals fails even to mention Baker's econometric studies, much less discuss why the district court's reliance on it was misplaced. Significantly, the FTC, which has made extensive use of econometric evidence in other recent merger cases,[16] failed to offer any econometric evidence to rebut Baker's studies.

Second, the court of appeals held that the district court's finding was inconsistent with its conclusion that there was a single, nationwide market for baby food that included all three brands, since this necessarily meant that consumers would switch among brands in response to a small, but significant, nontransitory increase in price (SSNIP).[17] This argument elevates form over substance. No one disputed that if all three brands were on the same shelf, consumers would find them close enough substitutes so as to switch among them in response to a SSNIP. But, as the district court found and the court of appeals did not contradict, Heinz and Beech-Nut are almost never on the same shelf and are rarely sold even in the same metropolitan area. That being the case, it is hard to understand how they could constrain each other's retail prices.

Third, the court of appeals held that the district court committed an error of law because it did "not take into account" the merger's elimination of competition at the wholesale level "between the only two competitors for the 'second shelf' position."[18] Observing that no court had ever held that a reduction in competition at the wholesale level is irrelevant unless plaintiffs can prove impact at the consumer level, the court held that the antitrust laws "*assume*" that a retailer faced with an increase in cost "will try so far as competition allows to pass that cost on to its customers in the form of a higher price for its products" and that it was error for the district court to require the FTC to prove the likelihood of such a pass-on with "certainty."[19]

This is yet another instance of the court of appeals substituting its own assumptions for what the evidence showed. The district court's finding that fixed trade allowances paid to get on the retail shelf were not passed on to consumers in the form of lower retail prices was based on both economic logic and an econometric study which found exactly that. The court of appeals cites no evidence to the contrary. As the Supreme Court held in *Eastman Kodak Co. v. Image Technical Services*[20] and again in *California Dental Association v. FTC*,[21] a court's assumptions about likely competitive effects cannot substitute for the empirical evidence of anticompetitive harm the antitrust laws require.

In these circumstances blocking a merger in order to preserve "competition" at the wholesale level for its own sake comes dangerously close to condemning a merger because it is efficient, much as the Supreme Court did in *Procter & Gamble*. To the extent it takes the form of fixed trade spending, competition between two brands to get on the retail shelf simply takes money from the manufacturer's pockets and puts it into the retailers. Since as one of Professor Baker's econometric studies showed, these fixed payments are not passed on to baby food customers in the form of lower retail prices, their only effect in the baby food market is to raise the cost of distribution for those smaller manufacturers who must pay such allowances.[22] By reducing or eliminating the need to pay for shelf space, the Heinz/Beech-Nut merger would have brought the merged firm's distribution costs more in line with Gerber's (which did not have to pay such allowances), making the merged firm more competitive with the market leader. This would have been more likely to drive prices down, thereby benefiting consumers, than to have led to higher prices. The evidence shows that this benefit was not simply a theoretical possibility. The district court found that there tends to be an inverse relationship between fixed and variable trade spending;[23] this means that in those markets where Heinz and Beech-Nut have to spend more just to get on the shelf they are likely to have less money for the variable trade spending to support couponing and other discount programs that are passed onto consumers. This is a reason to permit the merger, not prohibit it.

I anticipate two objections to this last assertion: first, that monopsony buying power is objectionable under the antitrust laws even where it may reduce downstream prices because it harms allocative efficiency; second, that it amounts to an argument that we should sacrifice competition for efficiency, which is a value judgment for legislatures, not courts, to make.[24] Neither objection is valid. Baby food competes with hundreds, if not thousands, of other categories of products for retail shelf space, so even a baby food monopolist would have no monopsony buying power in the market for retail shelf space. Moreover, by making Heinz a closer competitor to Gerber, the merger, far from eliminating bidding among baby food makers for shelf space, is more likely to extend that bidding competition across the entire range of baby food makers, including Gerber, who is now free of it. To the extent bidding for shelf space enhances allocative efficiency, the merger will, therefore, improve allocative efficiency, not harm it.

***Coordinated Effects.*** The district court had also found that "the normal presumption that increases in concentration will increase the likelihood of tacit collusion" was rebutted in this case by the presence of "structural market barriers to collusion" in the retail market for jarred baby food.[25] In so finding, the district court again relied on Baker's expert testimony. He testified that because of the efficiencies that would be realized from the merger, Heinz would have an increased incentive and ability, post-merger, to increase its market share and that this would make cartel behavior more difficult because it would make it harder for the two remaining firms, Heinz and Gerber, to reach consensus on price and output. This led him to conclude that at least 50 percent (and perhaps all) of the cost savings resulting from the merger were likely to be passed on to consumers, resulting in as much as a 15 percent reduction in quality-adjusted retail prices.[26]

The court of appeals disagreed. It found that because the district court had "failed to specify any 'structural barriers to collusion' that were unique to the baby food industry, its conclusion that the ordinary presumption of collusion in a merger to duopoly was rebutted was clearly erroneous."[27] The court buttressed this conclusion by referring, without citation, to "record evidence of past price leadership in the baby food industry."[28]

Once again, it is difficult to understand the reasoning behind the appellate court's decision. Contrary to its statement, at the retail level in most local markets the proposed transaction was not a merger to duopoly because, in all but a handful of metropolitan areas, the market structure was already a duopoly, with only two brands present on retail shelves. The only sense in which the transaction could be characterized as a merger to duopoly at the retail level is that it eliminated the threat of potential entry into these two-firm local markets by the third national manufacturer of baby food. There was no evidence in the record, however, that such entry was likely, much less that the threat of entry operated to constrain retail prices.[29]

Equally seriously, if the court of appeals was right that Gerber, faced with competition from two smaller, inefficiently-sized competitors, was already acting as a price leader, it is by no means obvious that combining the two smaller competitors would facilitate coordination leading to higher prices. To the contrary, to the extent the merger reduced the costs or enhanced the quality of the number two firm, prices might well fall, even if the allegedly ongoing coordinated behavior continued. As basic price theory teaches, even a monopolist's profit-maximizing price will be reduced as a result of lower costs; the same is equally true for oligopolistically determined prices.

***Efficiencies.*** Turning to efficiencies, the court of appeals began by noting that while "the Supreme Court has not sanctioned the use of efficiencies in a section 7 case . . . , the trend among lower courts is to recognize the defense."[30] The court held, however, that the high market concentration levels present in this case required, in rebuttal, proof of "extraordinary" efficiencies.[31] This assertion merits closer examination. The principal support the court cites for this principle is *Areeda & Hovenkamp*.[32] But in the very section of their treatise the court cites, *Areeda & Hovenkamp* say they "would permit the proof to be relaxed somewhat when neither of the merging firms is the largest firm in the market and the evidence shows that prior to the merger the merging firms both had higher costs than at least one larger rival, and that the merger will bring the costs of the postmerger firm more into line with those of the rival."[33] They note, in addition, that the case for an economics defense is particularly strong where market demand is declining, stable or growing very slowly.[34] *Areeda & Hovenkamp* could not have better described the situation faced by Heinz and Beech-Nut. In addition, the court's insistence that the parties demonstrate "extraordinary efficiencies" rests on the premise that the merger posed grave danger to competition. For the reasons discussed above, this premise is open to serious question.

Applying its questionable "extraordinary efficiencies" standard, the court goes on to hold that the district court's analysis fell short of the findings necessary for a successful efficiencies defense. In so holding, the court pointed to four specific failings, but in each case it is the court of appeals' critique, not the district court's analysis, that is flawed.

Focusing first on the manufacturing cost savings claimed by the parties, the court minimizes the significance of those savings by showing that they amounted to *only* 22.3 percent of Beech-Nut's total variable manufacturing costs and would be even less as a percent of the new entity's entire production, which it held was the relevant figure, citing *Areeda & Hovenkamp*.[35] In so ruling, the court overlooked that *Areeda & Hovenkamp* added the important qualification that this measure ought not apply to an efficient firm's acquisition of an inefficient firm and that such an acquisition "may be justifiable when the acquisition significantly reduces the cost of producing the inefficient firm's output and that enables efficient production to be carried over a larger output."[36]

More generally, the court of appeals' rejection of variable cost savings of the magnitude present in this case without any effort to quantify the price increases likely to result from the merger is analytically questionable. Doing so seems inconsistent both with the traditional rule of reason balancing test and the approach taken by the agencies in the Horizontal Merger Guidelines. Under the rule of reason, the courts are required to balance the potential efficiencies against the anticompetitive injury, with plaintiffs bearing the ultimate burden of proving that the harms outweigh the benefits.[37] Similarly, the Merger Guidelines provide that the agencies will examine whether the cognizable efficiencies "would be sufficient to reverse the merger's potential to harm consumers in the relevant market, e.g., by preventing price increases in that market."[38] As this illustrates, an evaluation of the size of the efficiencies cannot take place in a vacuum, but requires balancing whatever price increase the court finds is likely to result from an increase in market power against the price decrease that is likely to flow from the expected efficiencies—exactly the tradeoff Williamson described three decades ago. In *Heinz*, the court of appeals made no effort to quantify the likely price increase that might be caused by the merger, making it impossible to judge the likely net effect of the merger on prices. The only evidence in the record bearing on that issue was Baker's testimony that because the merger was likely to intensify, not diminish, competition between Heinz/Beech-Nut and Gerber, at least 50 percent (and perhaps all) of the cost savings would be passed onto consumers, resulting in as much as a 15 percent reduction in the quality-adjusted price of baby food.[39]

The court of appeals next focused on and rejected the district court's finding that the merger would allow the parties to realize substantial distribution efficiencies. In so doing, the court of appeals made an appellate finding that Beech-Nut could make its distribution system more efficient without the merger, arguing that the fact that Heinz had been able to develop a more efficient system showed that a firm of Beech-Nut's size need not merge to attain an efficient distribution system.[40] Here, the court of appeals appears to be forgetting that Heinz manufactures and distributes a broad range of other products in addition to baby food ("Heinz 57 varieties" is, after all, the company slogan). Heinz's ability to develop an efficient distribution system for its broad range of products hardly shows that a single product company like Beech-Nut could do likewise just because its volume of baby food sales is similar.

Next, repeating the unexceptionable mantra that efficiencies must be merger specific, the court of appeals held that the efficiencies claimed by the parties were not "cognizable" (a term it borrows from the Merger Guidelines) because the district court "never explained why Heinz couldn't realize efficiencies without merger."[41] In reaching this conclusion, the court maintains that the principal merger benefit claimed by Heinz was access to Beech-Nut's better recipes and that Heinz's counsel at oral argument could not explain why Heinz couldn't simply use the money it was spending to buy Beech-Nut to develop better recipes on its own. There are two problems with this argument.

First, the court of appeals misconstrued the nature of the efficiencies being claimed. Most of the efficiencies the district court found related to diseconomies faced by *Beech-Nut*, not *Heinz*. Even were it true that Heinz could develop better recipes on its own, that would do nothing to bring Beech-Nut's costs more in line with its more efficient rivals.

Second, as the testimony before the district court showed, Heinz's ability to expand is hampered, not so much by inferior recipes for baby food, but by the strong brand preferences of consumers for Beech-Nut and Gerber. As *Areeda & Hovenkamp* recognize, internal expansion is often not an attractive alternative in the face of strong consumer preferences for other brands because the stronger the brand preference, the more the firm seeking to expand would have to reduce prices to attract consumers away from other brands.[42]

More generally, the court of appeals decision overestimates the ease with which firms can capture the efficiencies of a merger through internal expansion and pays inadequate attention to the relative costs of the two alternatives. Since economic theory teaches that firms always seek to maximize their profits, one can presume that if internal expansion were a profit maximizing strategy, the merging firms would already have undertaken such expansion up to the point where it was no longer profitable. This presumption is particularly strong here where multiple owners of Beech-Nut had consistently over a period of several decades concluded that building a new, more efficient plant would not be profit maximizing.

*Areeda & Hovenkamp* provide an excellent discussion of why internal expansion is likely, in cases like Beech-Nut and Heinz, to be significantly more costly than merger.[43] As they point out, an efficiency should be viewed as merger specific if it could not readily be attained by other means *or* if the social cost of attaining it by other means is at least as high as the social cost of the merger. *Areeda & Hovenkamp* show that, taking these relative social costs into account, internal expansion is not always clearly preferable, even where it is feasible, for at least five reasons. First, as in the case of Heinz and Beech-Nut, the merging firms might possess nicely complementary resources, which could be integrated in ways that would be far more costly for either firm to attempt independently. Second, even if either firm could achieve similar economies independently, doing so may take them much longer. Third, where buying is cheaper than building, the efficiency-creating move might not be made at all. Fourth, construction of new facilities may involve social waste if they duplicate resources that end up having to be scrapped rather than merged. (This would appear to have been the case here; had Beech-Nut tried to build a new, more efficient plant, Heinz's existing excess capacity would continue to go unused.) Fifth, adding capacity in an industry that already has sufficient capacity puts downward pressure on price and may drive price below a competitive level; because of this "capacity effect," internal expansion may be an unattractive route to efficiencies. Again, this would appear to be the case here, given the declining demand for baby food and Heinz's existing excess capacity.

*Areeda & Hovenkamp* conclude that, given all this, the alternative to a merger of two inefficiently sized firms may not be internal expansion by both but rather expansion by one and exit by the other. In such a case (which the Heinz/Beech-Nut merger may have been), the construction of a new facility by one firm may be a social waste when the facilities of the existing firm could have been used instead. In addition, in these circumstances a merger would not worsen price competition since the number of competitors remaining at the end of the day will be the same under either alternative.

I can anticipate an argument that even if internal expansion were not likely, other, less anticompetitive alternatives might be available, such as a toll manufacturing arrangement pursuant to which Heinz would use its excess capacity to produce for Beech-Nut. It is by no means clear, however, that such an arrangement would be in Heinz's strategic interest even were the merger disapproved or, even if it were, that the results would be any better from a consumer welfare perspective than a full merger. Contractual joint ventures among competitors are notoriously difficult to arrange and administer and often entail large transactions costs. In any event, had the FTC advanced that alternative, it would have required close examination; since it apparently was not advanced, there is nothing in the record to suggest what such scrutiny would have found.

In sum, what the court of appeals overlooked in applying too stringent a "merger specific" test is that forcing the smaller firms in a market to expand by internal expansion, rather than by merger, imposes social costs, even if the firms are ultimately able to do so. It also risks such expansion never occurring, leaving the status quo in which a single firm (Gerber) is able to continue to maintain its dominant position without serious challenge from its smaller competitors.

Finally, the court of appeals discounted the district court's finding that the merger would facilitate innovation, making it easier for the merged firm to introduce new products by spreading the expense of promoting and marketing those products over a larger volume base. The district court based this finding on testimony by Jonathan Baker, who relied in turn on an analysis prepared for Heinz by Booz Allen showing that it needed to be present on 70 percent or more of supermarket shelves in order for a new product launch to be profitable. The court of appeals, again resorting to appellate fact-finding, discounted this analysis on the ground that one year was too small a sample,[44] while ignoring testimony from Heinz's CEO corroborating that Heinz would not provide marketing support to a new product unless it was on more than 80 percent of shelves.[45] The court again cites *Areeda & Hovenkamp*, this time for the proposition that "the case for recognizing a defense based on promotional economies is relatively weak."[46] But once again, the court of appeals takes a sentence fragment from *Areeda & Hovenkamp* out of context. They go on in the same paragraph to say that the reason savings in promotional expenses will rarely justify an otherwise anticompetitive merger is that promotional expenses are generally small relative to the cost of the product, and that there should, therefore, be an exception for certain highly promoted products, such as ready-to-eat breakfast cereals, for which promotional expenses may equal the cost of raw materials and direct production.[47] The court failed even to consider whether baby foods might be such a product.

## Concluding Observations

The court of appeals decision in *FTC v. H.J. Heinz Co.* is another in a growing line of lower court decisions accepting, without necessarily holding, that efficiencies may in appropriate circumstances be a defense to an otherwise anticompetitive merger. The *Heinz* decision illustrates, however, that the courts remain highly skeptical of parties' efficiencies claims. Any party seeking to advance such claims should, therefore, recognize that they will carry a heavy burden as to all three of the critical elements of the claims: first, in showing that the efficiencies are substantial; second, in showing that they are merger specific; and, third, in showing that they will serve to maintain prices and output at premerger levels or better.

1 FTC v. Proctor & Gamble Co., 386 U.S. 568 (1967).

2 Oliver Williamson, *Economies as an Antitrust Defense: The Welfare Tradeoff*, 58 Am. Econ. Rev. 18 (1968).

3 *Id.* at 34.

4 U.S. Dep't of Justice, Merger Guidelines (1982), *reprinted in* 4 Trade Reg. Rep. (CCH) ¶ 13,102.

5 *See* FTC v. University Health, 938 F.2d 1206, 1222 (11th Cir. 1991) ("whether an acquisition would yield significant efficiencies in the relevant market is an important consideration in predicting whether the acquisition would lessen competition").

6 246 F.3d 708 (D.C. Cir. 2001).

7 FTC v. H.J. Heinz Co., 116 F. Supp.2d 190 (D.D.C. 2000).

8 See United States v. Philadelphia Nat'l Bank, 324 U.S. 321 (1963).

9 *Commission Override Staff, Vote to Block Beech-Nut Sale*, FTC: Watch, July 10, 2000.

10 *Id.*

11 FTC v. H.J. Heinz Co., 116 F. Supp. 2d 190 (D.D.C. 2000).

12 *Id.* at 201. On appeal, the FTC argued (contrary to its earlier stipulation) that a preliminary injunction would not necessarily kill the merger and the court of appeals so held, noting that the district court had pointed to no evidence to support its contrary conclusion. *See Heinz*, 246 F.3d at 710. This is another illustration of the procedural unfairness of appellate factfinding; since the parties had stipulated to this finding, there was no reason for the district court to cite any evidence supporting it.

13 United States v. Philadelphia Nat'l Bank, 374 U.S. 321 (1963).

14 *Heinz Co.*, 246 F.3d at 718. The court of appeals' reliance on the district court's oversight as the sole basis for holding the district court's findings of fact clearly erroneous was itself arguably an error of law. *See In re* Baby Food Litigation, 166 F.3d 112, 131 (3d Cir. 1999) ("The District Court may not have specifically addressed this testimony but that does not mean the court ignored it.").

15 The hazards of appellate factfinding in these circumstances are self-evident. The only witness whose testimony the court of appeals cites to support its finding that Heinz and Beech-Nut depress each other's prices where both are present in the same area was able to identify only a single instance where that had happened and admitted on cross examination that in a number of other instances it had not. *See* Tr. 147–48, 166.

16 *See, e.g.*, FTC v. Staples, Inc., 970 F. Supp. 1066 (D.D.C. 1997).

17 *Heinz*, 246 F.3d at 718.

18 *Id.* at 719.

19 *Id.*

20 504 U.S. 451 (1992).

21 526 U.S. 756, 775 n.12 (1999).

22 While the court of appeals may be right that, to the extent there is competition among retailers, these fixed trade allowances may be passed onto retail grocery shoppers generally in the form of wider aisles and the like, this benefit is in a different market from the market for baby food.

23 *Heinz*, 116 F. Supp. 3d at 197.

24 *See, e.g.*, National Soc'y of Prof'l Eng'rs v. United States, 435 U.S. 679, 695 (1978) ("the statutory policy precludes inquiry into the question whether competition is good or bad").

25 *Heinz*, 116 F. Supp. 2d at 198.

26 Tr. 942–43.

27 *Heinz*, 246 F.3d. at 725.

28 *Id.* at 724.

29 In fact, the Third Circuit in *In re Baby Food Antitrust Litigation*, 166 F.3d 112, 127 (3d Cir. 1999), found, to the contrary, that refraining from such entry would be "rational competitive conduct" given that entry "required substantial capital expenditures and resource commitments" and the incumbents "could aggressively respond to . . . territorial expansion in the expanded areas and in other territories [in a way] that might prove the expansion to be eruptive, destructive, and expensive."

30 246 F.3d. at 720. The court of appeals carefully refrained, as have most other courts that have examined the issue, from affirmatively holding that efficiencies can be a defense to an otherwise unlawful merger, not having to reach that issue because it found the efficiencies insufficient to justify the merger even if such a defense existed. *See, e.g.*, FTC v. Cardinal Health, Inc., 12 F. Supp. 2d 34, 61 (D.D.C. 1998); FTC v. Staples, Inc., 970 F. Supp. 1066, 1088–1091 (D.D.C. 1997).

31 *Id.*

32 4A Phillip E. Areeda, Herbert Hovenkamp & John L. Solow, Antitrust Law (rev. ed. 1998) [hereinafter cited as Areeda & Hovenkamp].

33 *Id.* ¶ 971f, at 44–45.

34 *Id.* ¶ 973b9, at 57.

35 *Id.* ¶ 976d, at 93–94.

36 *Id.* ¶ 976b2, at 90.

37 *See generally* ABA Section of Antitrust Law, Antitrust Law Developments 51–71 (4th ed. 1996).

38 U.S. Dept. of Justice & Federal Trade Comm'n, Horizontal Merger Guidelines § 4.0 (1997), reprinted in 4 Trade Reg. Rep. (CCH) ¶ 13, 104.

39 Tr. 942–43

40 *Heinz*, 246 F.3d at 721.

41 *Id.* at 721.

42 Areeda & Hovenkamp ¶ 973 at 54.

43 *Id.*

44 The court's action in discounting this study because of its small sample size is ironic given its own reliance on anecdotal evidence to overcome Professor Baker's three econometric studies.

45 Tr. 442.

46 *Heinz*, 246 F.3d at 723 (quoting Areeda & Hovenkamp ¶ 975f).

47 Areeda & Hovenkamp ¶ 975f, at 77.