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Breaking the Vicious Cycle: Establishing a Gold Standard for Efficiencies

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I. Introduction

Good afternoon! Thank you to Bates White and George Rozanski for inviting me to speak, and for assembling such a strong panel to discuss merger efficiencies. Before I go any further, I must give the standard disclaimer: the views I express are my own and do not necessarily reflect the views of the Federal Trade Commission or of any other Commissioner.

I sometimes set the stage for my speeches and articles by hearkening back to a bygone antediluvian era in which, for example, regulation displaced the free market,[1] communism eliminated it entirely,[2] or a muddled antitrust regime pursued ever-changing goals.[3] In so doing, I hope to show how far we have come from our past mistakes, so that we do not repeat them. Unfortunately, this type of approach will not be effective for the topic I am addressing today. While there has been halting progress in the treatment of efficiencies, merger policy continues to be focused almost entirely on anticompetitive effects.[4] In other words, when it comes to efficiencies, we still live in the antediluvian era.

The overarching problem is that while courts and the U.S. antitrust Agencies – the Federal Trade Commission and Department of Justice – are comfortable with probabilistic assessments of merger harms, they seem to require certainty in efficiencies forecasts. For instance, in *Brown Shoe* the Supreme Court interpreted the Clayton Act's prohibition on mergers whose effect "may be substantially to lessen competition" as indicating that the Act is concerned with "probabilities, not certainties" and concluded that "[m]ergers with a probable

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[1] Christine S. Wilson & Keith Klovers, *The growing nostalgia for past regulatory misadventures and the risk of repeating these mistakes with Big Tech*, 8 J. ANTITRUST ENFORCEMENT 10 (2019).
[2] Christine S. Wilson, *Milton Friedman Is Still Right: Marking the 35th Anniversary of Free Markets for Free Men* (October 12, 2019), https://www.ftc.gov/system/files/documents/public_statements/1553170/wilson_-_cpac_brazil_remarks_10-12-19.pdf.
[3] Christine S. Wilson, Thomas J. Klotz & Jeremy A. Sandford, *Recalibrating the Dialogue on Welfare Standards: Reinserting the Total Welfare Standard into the Debate*, 26 GEO. MASON L. REV. 1435 (2019).
[4] Daniel A. Crane, *Rethinking Merger Efficiencies*, 110 MICH. L. REV. 347, 390 (2011) ("Merger policy has long been dominated by a focus on only one side of the ledger – anticompetitive effects.").

anticompetitive effect were to be proscribed."[5] Contrast this with the text of the Horizontal Merger Guidelines, which states that "[e]fficiency claims will not be considered if they are vague, speculative, or otherwise cannot be verified by reasonable means," and that "[p]rojections of efficiencies may be viewed with skepticism, particularly when generated outside of the usual business planning process."[6]

Under this asymmetric treatment, the Agencies and courts regularly condemn mergers based on vague suspicions of future coordination, suggestive business documents, or structural presumptions.[7] In contrast, efficiencies claims are viewed skeptically, apparently because they are seen as vague, suggestive, or presumed. The result is that evidence of likely efficiencies rarely, if ever, suffices to overcome a determination that anticompetitive effects may result from a merger.

Both the Horizontal Merger Guidelines and the law place the onus on merging parties to develop evidence of efficiencies. The information necessary to build an effective efficiencies presentation is necessarily spread across the two merging firms, which face antitrust limitations on the exchange of competitively sensitive information prior to the merger's consummation. Thus, an effective efficiencies presentation all but requires the creation of a clean team, often staffed in part with outside consultants.

If courts and the Agencies systematically discount efficiencies evidence, requiring certainty when none is possible, there is little incentive for merging firms to invest in expensive clean teams and consultants. While serving as FTC chairman, Tim Muris observed in 2002 that

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[5] *Brown Shoe Co., Inc. v. United States*, 370 U.S. 294, 323 (1962).
[6] U.S. Dep't of Justice & Fed. Trade Comm'n, Horizontal Merger Guidelines 30–31 (2010) [hereinafter Horizontal Merger Guidelines], https://www.ftc.gov/sites/default/files/ attachments/merger-review/100819hmg.pdf.
[7] *See* Douglas H. Ginsburg & Joshua D. Wright, *Philadelphia National Bank: Bad Economics, Bad Law, Good Riddance*, 80 ANTITRUST L. J. 201 (2015) (describing the rise and fall of the structural presumption in economics, and its continued legal influence).

antitrust attorneys sometimes advise merging firms not to bother with efficiencies analysis.[8] If, as a result, the overall quality of efficiencies presentations is low, courts and Agencies will lower the status of efficiencies evidence as a general matter, further eroding the incentive for merging parties to produce high quality evidence in the first place.

It is time for this vicious cycle to end, and I believe the Agencies are best positioned to lead us out of it. First, the Agencies should adjust their approach to treat evidence of efficiencies symmetrically with that of harms. Second, they should provide additional guidance to the antitrust bar and the business community about what types of efficiencies analysis will and will not meet their standards. In this speech, I suggest that the Agencies publish "gold standard" efficiencies analyses through one or more hypothetical cases accompanied by exhibits, explanations and guidance designed to amplify the language in the Horizontal Merger Guidelines. The goal is to establish a benchmark identifying what is needed for an efficiency to be deemed cognizable, and to commit the Agencies to crediting meritorious claims in the future.

Merging parties are in possession of most information that would allow the Agencies to evaluate efficiencies likely to result from a merger, so I am not disputing that parties should bear the burdens of production and proof on efficiencies. However, a more reasonable standard and clear guidance will incentivize higher quality efficiencies analyses in more cases, which in turn will at least gradually shift the priors of courts and the Agencies towards greater acknowledgement of efficiencies, even those that are no more certain than the harm that would be created by a merger.

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[8] Timothy J. Muris, *Understanding Mergers: Strategy and Planning, Implementation, and Outcomes* (December 9, 2002), https://www.ftc.gov/public-statements/2002/12/understanding-mergers-strategy-and-planning-implementation-and-outcomes.

II. Treatment of Efficiencies by Courts and the Agencies, 1950-2020

In the first two decades following the 1950 amendments to the Clayton Act, judicial opinions *did* achieve a perverse symmetry in their treatment of merger efficiencies and anticompetitive effects: they viewed both as harms. In *Brown Shoe*, vertical integration between a wholesaler and retailer was deemed illegal because the resulting savings would have allowed the merging firms to "market their own brands at prices below those of competing independent retailers."[9] While the Court acknowledged that consumers would benefit from lower prices, it determined that the purpose of the Clayton Act was to promote "decentralization," even at the expense of "occasional higher costs and prices."[10]

Only one year after *Brown Shoe*, the Court appeared to moderate its view towards merger efficiencies from hostility to mere indifference. In *Philadelphia National Bank*, it found that an otherwise anticompetitive merger "is not saved because, on some ultimate reckoning of social or economic debits and credits, it may be deemed beneficial."[11] Four years later, in *Procter & Gamble*, the Court determined that allowing Procter & Gamble to purchase Clorox would allow the merged firm to benefit from advertising efficiencies that, in its view, would discourage entry. As to whether these efficiencies were a good or bad thing, the Court stated that "possible efficiencies cannot be used as a defense to illegality."[12] Lower courts have viewed merger cost savings as harms as recently as the 1970s.[13]

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[9] *Brown Shoe*, 370 U.S. at 344. I note that the discussion of merger efficiencies in this speech does not apply to the elimination of double marginalization, an inherent procompetitive effect that typically arises from vertical mergers.
[10] *Id.*
[11] *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321, 371 (1963).
[12] *FTC v. Procter & Gamble Co.*, 386 U.S. 568, 580 (1967).
[13] *U.S. Steel Corp. v. FTC*, 426 F.2d 592 (6th Cir. 1970) (concluding that a vertical merger was anticompetitive in part because it would confer "decisive cost advantages over non-integrated competitors."); *Mississippi River Corp. v. FTC*, 405 U.S. 562 (1974) (finding that a series of vertical mergers was anticompetitive in part because it had an "immediate[]" and "adverse" impact on a rival "local business.").

To be sure, there were green shoots even in this early era. The DOJ's 1968 Merger Guidelines, issued during the tenure of Assistant Attorney General Donald Turner and influenced by work that Oliver Williamson had begun as a DOJ employee, incorporated a limited efficiencies defense, effectively breaking with the Supreme Court.[14] Six years later, the Court's 1974 *General Dynamics* decision found that merging parties had rebutted the government's *prima facie* case, and is sometimes seen as opening the door to efficiencies defenses.[15] Merging parties began making serious efficiencies arguments to the Agencies in the late 1970s, and by the early 1980s each Agency appears to have closed an investigation in part because of efficiency considerations.[16] The DOJ's 1984 Merger Guidelines improved the efficiencies language and moved it to the section on competitive effects.[17]

Progress seems to have slowed since the 1980s. While the 1992 Horizontal Merger Guidelines removed a requirement that the parties present "clear and convincing proof" of efficiencies, only one year prior the FTC argued to the U.S. Court of Appeals for the Eleventh Circuit that the law did not permit an efficiencies defense.[18] The FTC repeated this argument in 1997, this time to the Sixth Circuit.[19] While both appellate courts disagreed with the FTC's view of efficiencies,[20] by 1998 the agency was back at it in a district court, questioning whether an

[14] See William J. Kolasky & Andrew R. Dick, *The Merger Guidelines and the Integration of Efficiencies into Antitrust Review of Horizontal Mergers*, 71 ANTITRUST L.J. 207, 213 (2003).
[15] *U.S. v. General Dynamics Co.*, 415 U.S. 486 (1974); Kolasky & Dick at 214 ("That decision gave rise to what came to be known (somewhat loosely) as the "*General Dynamics* defense" and encouraged parties to begin advancing efficiency claims.").
[16] Kolasky & Dick, *supra* note 14, at 214-215.
[17] *Id*. at 220.
[18] *FTC v. University Health, Inc.*, 938 F. 2d 1206, 1222 (11th Cir. 1991) ("The appellees argue that the proposed acquisition would generate significant efficiencies and, therefore, would not substantially lessen competition. The FTC responds that the law recognizes no such efficiency defense in any form.").
[19] *FTC v. Butterworth Health Corp.*, No. 96-2440 (6th Cir. July 8, 1997) (per curiam).
[20] Kolasky & Dick, *supra*, note 14, at 232 ("the [Eleventh Circuit] held that efficiencies should not be a defense to a merger that was found to be anticompetitive, but should be instead integrated into the competitive effects analysis, where they could be used to rebut a prima facie case"); at 232-233 ("the Sixth Circuit rejected an FTC argument that the district court had committed legal error in allowing the merging hospitals to rebut the FTC's prima facie case with evidence of efficiencies.").

efficiencies defense was allowed at all.[21] In 1999, future FTC Chairman Tim Muris characterized the Agencies' attitude towards efficiencies, at least in litigated cases, as one of "unrelenting hostility."[22]

Despite the FTC's persistent efforts, by the turn of the century at least some courts had made it clear that merging parties in theory could redeem an otherwise anticompetitive merger by demonstrating cognizable efficiencies.[23] In practice, the bar for doing so always seemed to be just out of reach. Section 4 of the 1997 Horizontal Merger Guidelines, ostensibly with the goal of more thoroughly explaining current practice, introduced the language of merger specificity, verifiability, and cognizability.[24] However, these concepts seemed to provide additional ammunition for the Agencies and courts to shoot down efficiency claims.

A survey of FTC staff recommendation memoranda to the Commission written between 1999 and 2007 found that 79% of memos considered at least one efficiencies claim, and that the average case had claimed efficiencies equal to 8.1% of the transaction's reported value.[25] However, the Bureau of Competition accepted only 29 out of 342 claims it considered, while the Bureau of Economics accepted 84 out of 311.[26] In 2009, future FTC Chairman Joe Simons and Professor Daniel Crane observed that "to the extent [the Agencies] talk about efficiencies, it

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[21] *FTC v. Cardinal Health, Inc.*, 12 F. Supp. 2d 34 (D.D.C 1998).

[22] Timothy J. Muris, *The Government and Merger Efficiencies: Still Hostile after All These Years*, 7 GEO. MASON L. REV. 729, 751 (1999).

[23] *US v. Baker Hughes Inc.*, 908 F. 2d 981, 984-986 (D.C. Cir. 1990) (noting multiple defendants' success in rebutting the government's prima facie case by presenting evidence on non-entry factors; citing P. Areeda & H. Hovenkamp, Antitrust Law, and L. Sullivan, Handbook of the Law of Antitrust, as hornbook law that such factors include the prospect of efficiencies from merger; noting that the Department of Justice's 1984 Merger Guidelines § 3.5 also include efficiencies as such a factor); *University Health*, 938 F. 2d at 1222 ("in certain circumstances, a defendant may rebut the government's prima facie case with evidence showing that the intended merger would create significant efficiencies in the relevant market."); see infra n. 31.

[24] Kolasky & Dick, *supra* note 14, at 226-227.

[25] Malcolm B. Coate & Andrew J. Heimert, *Merger Efficiencies at the Federal Trade Commission 1997-2007* (February 2009), https://www.ftc.gov/reports/merger-efficiencies-federal-trade-commission-1997-2007.

[26] *Id.* at 16 (describing Table 2: "the aggregate data show that the BC memoranda discussed a total of 342 efficiency claims, rejecting 109 and accepting 29 [. . .]; at 22, describing Table 3: "BE staff accepted 84 efficiencies claims (27.0 percent) and rejected 37 claims (11.9 percent).").

tends to be in a derogatory way[…] The only real significance of efficiencies today seems to be as evidence that something other than market power motivated the transaction."[27] Consistent with this view, the FTC's staff memoranda were far more likely to credit efficiencies when recommending an investigation be closed than when recommending a complaint.[28]

The 2010 Horizontal Merger Guidelines largely imported the efficiencies language of the 1997 Guidelines. At the same time, they diminished the importance of market definition in favor of upward pricing pressure analysis, which some commentators saw as likely to lead to narrower markets.[29] As I have argued elsewhere, the combination of narrower markets and *Philadelphia National Bank*'s misguided prohibition on out-of-market efficiencies raises even further the legal and evidentiary hurdles a defendant must clear when seeking to prove offsetting procompetitive efficiencies.[30]

While several litigated cases have been decided at least partially on efficiency grounds,[31] courts largely continue to follow the Agencies' lead in minimizing the importance of

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[27] Joseph J. Simons & Daniel A. Crane, *Comments to the Federal Trade Commission and Department of Justice Antitrust Division, Unified Merger Analysis: Integrating Anticompetitive Effects and Efficiencies, and Emphasizing First Principles* (November 2009), https://www.ftc.gov/sites/default/files/documents/public_comments/horizontal-merger-guidelines-review-project-545095-00007/545095-00007.pdf.

[28] Coate & Heimert, *supra* note 25 at 16 (summarizing that in BC memos "[e]fficiency claims were accepted in 4.2 percent of the settled matters, 6.9 percent of the PI matters, and 15.3 percent of the closed cases."; at 22, summarizing that in BE memos "[e]fficiencies appear more likely to be accepted in closed matters (36.8 percent) than in PI matters (28.1 percent) or matters resulting in a consent decree with the merging firms (18.3 percent).").

[29] Judd E. Stone & Joshua D. Wright, *The Sound of One Hand Clapping: The 2010 Merger Guidelines and the Challenge of Judicial Adoption*, 39 REV. INDUS. ORG. 145, 150 (2011) ("Observers generally agree that the 2010 Guidelines' methodological approach will result in narrower product markets.").

[30] Christine S. Wilson, *The Unintended Consequences of Narrower Product Markets and the Overly Leveraged Nature of Philadelphia National Bank* (June 30, 2019), https://www.ftc.gov/system/files/documents/public_statements/1532894/wilson_-_remarks_at_oxford_antitrust_enforcement_symposium_6-30-19_0.pdf.

[31] *See, e.g.*, *FTC v. HJ Heinz Co.*, 116 F. Supp. 2d 190, 198 (D.D.C. 2000), rev'd, 246 F.3d 708 (D.C. Cir. 2001) ("My conclusion in this case does not rest upon aspirational testimony, but instead credits powerful evidence in the record about the efficiencies realized by the merger, and about the enhanced prospects of the merged entity to introduce innovative products to compete with Gerber. That evidence, in my view, shows that the Commission's prima facie case inaccurately predicts the merger's probable effect on future competition."); *FTC v. Butterworth Health Corp.*, 946 F.Supp. 1285, 1300-01 (W.D. Mich. 1996), aff'd, 121 F.3d 708, (6th Cir. 1997) ("In sum, the Court is persuaded that the proposed merger would result in significant efficiencies… and represents savings that

efficiencies.[32] One study surveyed merger cases from 1986 to 2009 and found that "[a]lthough courts claim to be balancing merger-generated efficiencies with other negative factors affecting market competition," they are actually "making an assessment of the relevant concentration in the applicable market and then allowing that initial assessment to color their recognition of claimed efficiencies."[33] Indeed, even when courts acknowledge efficiencies in finding in favor of merging parties, they often emphasize that efficiencies were not pivotal to their decision.[34]

III. Asymmetry

Judicial and Agency skepticism towards efficiencies might be tolerable, or even desirable, were it paired with a similar skepticism towards merger price effects. For mergers reviewed before consummation, the analyses of both are inherently forward-looking and thus necessarily speculative. Just as efficiencies analysis relies on best guesses based on incomplete data, an analysis of merger price effects depends on modelling assumptions, imperfectly

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would, in view of defendants' nonprofit status and the Community Commitment, invariably be passed on to consumers.").

[32] *See, e.g.*, Joint Statement on the Burden of Proof at Trial at ¶ 11, *United States v. AT&T, Inc.*, No. 1:17-cv-02511-RJL (D.D.C. Mar. 13, 2018), ECF No. 87 (United States' Position: "No court has ever found efficiencies that justified the anticompetitive effects of a merger. As a result, the law is unsettled as to whether defendants can defeat a Section 7 case merely by showing the merger creates efficiencies, even if they 'outweigh' the anticompetitive effects proven by the plaintiff."); *FTC v. Penn State Hershey Med. Ctr.*, 838 F.3d 327, 347 (3d Cir. 2016) ("We note at the outset that we have never formally adopted the efficiencies defense. Neither has the Supreme Court. Contrary to endorsing such a defense, the Supreme Court has instead, on three occasions, cast doubt on its availability."); *id.* at 348 (concluding that, regardless of whether an efficiencies defense is available, defendants failed to satisfy requirements); *St. Alphonsus Med. Ctr.-Nampa Inc. v. St. Luke's Health Sys., Ltd.*, 778 F.3d 775, 788-91 (9th Cir. 2015) (same); *FTC v. H.J. Heinz Co.*, 246 F.3d 708, 720 (D.C. Cir. 2001) (same). *But see New York v. Deutsche Telekom AG*, No. 19 Civ. 5434 (VM), 2020 WL 635499, at *19-26 (S.D.N.Y. Feb. 11, 2020) (noting "uncertainty in the state of the law" but concluding that efficiencies were one factor justifying merger).

[33] Jamie Henikoff Moffitt, *Merging in the Shadow of the Law: The Case for Consistent Judicial Efficiency Analysis*, 63 VAND. L. REV. 1697 (2010).

[34] See *U.S. v. AT&T Inc.,* 310 F. Supp. 3d 161, 191 n.17 (D.D.C. 2018) (saying despite the court's confidence "that defendants will achieve considerable efficiencies beyond those conceded by the Government," the ruling "does not turn on the efficiencies offered by defendants in their affirmative case, but rather on its conclusion that the Government's evidence, as undermined and discredited by defendants' attacks, is insufficient to show a probability of substantially lessened competition, and thus that the Government has failed to carry its ultimate burden of persuasion."); *New York v. Deutsche Telekom AG et al*, No. 1:2019cv05434 - Document 409 (S.D.N.Y. 2020) ("mindful of the uncertainty in the state of the law regarding efficiencies and Plaintiff States' pertinent criticisms, the Court stresses that the Proposed Merger efficiencies it has recognized constitute just one of many factors that it considers and do not alone possess dispositive weight in this inquiry.").

measured inputs, and business documents subject to interpretation. Neither type of analysis should be dismissed just because it is less than definitive.

I've already discussed how the Horizontal Merger Guidelines text and case law appear to set different standards for demonstrating harms and efficiencies. Unsurprisingly, these disparate standards appear to result in disparate treatment. The 2014 merger of Ardagh and St. Gobain, two glass container manufacturers, may best exemplify this asymmetry. The parties put forward evidence of cost savings that they claimed would have resulted from overhead reduction and operation synergies. The majority of the Commission dismissed the efficiencies as either not being merger specific, or as not having been verified.[35] The FTC's complaint alleged that "nearly all" of the claimed efficiencies were non-cognizable.[36] In contrast, then-Commissioner Josh Wright's view was that the expected efficiencies were six times greater in magnitude than likely unilateral price effects.[37] Wright saw it as impossible to reach the Commission's conclusion of likely price effects and zero efficiencies without applying an asymmetric standard, despite the majority's protests to the contrary.[38] Ardagh and the FTC settled prior to trial. As is typical of mergers that are abandoned or settled, the Agencies got the final word on efficiencies.

I have called in the past for a symmetric treatment of merger harms and efficiencies.[39] An asymmetric approach has the obvious potential consequence of preventing some procompetitive

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[35] *Statement of the Federal Trade Commission In the Matter of Ardagh Group S.A., Saint-Gobain Containers, Inc., and Compagnie de Saint-Gobain*, File No. 131-0087, (April 11, 2014), https://www.ftc.gov/system/files/documents/public_statements/568811/140411ardaghcommstmt.pdf.

[36] *Complaint, In the Matter of Ardagh Group S.A., Saint-Gobain Containers, Inc., and Compagnie de Saint-Gobain*, https://www.ftc.gov/sites/default/files/documents/cases/2013/07/130701ardaghcmpt.pdf.

[37] *Dissenting Statement of Commissioner Joshua D. Wright In the Matter of Ardagh Group S.A., and Saint-Gobain Containers, Inc., and Compagnie de Saint-Gobain* (April 11, 2014), https://www.ftc.gov/public-statements/2014/04/dissenting-statement-commissioner-wright-matter-ardagh-group-sa-saint.

[38] *Id.* at 5.

[39] *See* Christine S. Wilson, *Antitrust and Innovation: Still Not A Dynamic Duo?* (September 10, 2019), https://www.ftc.gov/system/files/documents/public_statements/1544179/wilson_-_remarks_seps_9-10-19.pdf.(calling for symmetric treatment of dynamic harms and dynamic efficiencies); Christine S. Wilson, *Sleepy Hollow and the Arrovian Legend: Is There a Generalizable Relationship Between Concentration and Innovation?* (September 12, 2019),

mergers that increase consumer welfare. Daniel Crane makes the intriguing argument that an asymmetric approach may also make it *harder* to litigate against genuinely anticompetitive mergers, as courts may compensate for asymmetry by applying an across-the-board efficiencies credit, or by requiring greater proof of anticompetitive effects.[40]

The asymmetric approach is particularly problematic given a recent trend towards litigating over smaller predicted price effects.[41] Some commentators have argued against a case-by-case efficiencies analysis.[42] As an alternative, some would account for likely efficiencies by requiring greater evidence of anticompetitive effects.[43] To the extent this view continues to influence the thinking of courts or the Agencies, pursuing mergers with smaller predicted price effects without adjusting the treatment of efficiencies further diminishes the role of efficiencies and increases the risk of overenforcement.

IV. Breaking the Vicious Cycle

Given the hostility of courts and the Agencies towards efficiencies, but not anticompetitive effects, it is unsurprising that the latter generally carry the day. Consequently, merging parties have little incentive to incur the expense of clean teams and consultants to

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https://www.ftc.gov/system/files/documents/public_statements/1544375/wilson_concurrences_nyc_remarks_9-12-19.pdf.

[40] Crane, *supra*, note 4, at 368-369.

[41] https://globalcompetitionreview.com/article/1214319/dg-comp-top-economist-zero-price-can-be-special-and-efficiencies-credible (summarizing BE Director Andrew Sweeting's remarks that the FTC now looks closely at mergers where its models predict relatively small anti-competitive effects, and that "means the FTC has to take efficiencies seriously so it does not block procompetitive deals."); *Statement of Commissioner Joshua D. Wright Dissenting in Part and Concurring in Part, In the Matter of Dollar Tree, Inc. and Family Dollar Stores, Inc.* (July 13, 2015), https://www.ftc.gov/system/files/documents/public_statements/681781/150713dollartree-jdwstmt.pdf (objecting to the Commission's requiring divestiture of some stores with a "gross upward pricing pressure index" of less than five percent, or indeed below any level, despite a strong legal and economic case for such a safe harbor).

[42] *See* Kolasky & Dick, *supra* note 14, at 213 (describing the reaction to the 1968 *Guidelines*); *see also* Alan A. Fisher & Robert H. Lande, *Efficiency Considerations in Merger Enforcement*, 71 CAL. L. REV. 1580 (1983) (describing problems with the case-by-case approach).

[43] *See* Joseph Farrell & Carl Shapiro, *Antitrust Evaluation of Horizontal Mergers: An Economic Alternative to Market Definition*, 10 THE B.E. J. OF THEORETICAL ECON. ART. 9 (2010) (at 10, referring to a "standard deduction" that would "credit some default marginal-cost efficiencies for each overlap product.").

document likely efficiencies. Nonetheless, merging parties typically do go through the motions of invoking efficiencies, on a quixotic quest to meet the lofty standard of cognizability. Then-FTC Chairman Tim Muris observed that these desultory efforts contributed to Agency skepticism of efficiencies, making the task of convincing Agency staff even more difficult for the next set of merging firms.[44]

We can do better. The current vicious cycle disincentivizes all sides – merging parties, Agencies, and courts – from engaging in a productive weighing of efficiencies against merger harms. I believe the Agencies are best positioned to lead us out of this cycle, just as the DOJ led us out of the era in which efficiencies were seen as irrelevant with its 1968 Merger Guidelines.

Allow me to describe what I view as the most productive path forward. The Agencies should put their cards on the table with clear, consistent standards for what does and does not constitute a cognizable efficiency. In doing so, they will encourage more robust and refined efficiencies analysis from merging parties. At the same time, they will have greater credibility when they dismiss efficiencies claims that fall short of these standards.

Merger policy is iterative, as each matter builds upon the examples of its predecessors. On efficiencies, as we have seen, these are very poor examples. Breaking the vicious cycle requires a new baseline. I would have the Agencies develop efficiencies analyses for one or more hypothetical cases, including hypothetical exhibits and party submissions. These hypothetical materials could be accompanied by guidance that amplifies the broad strokes on efficiencies painted in the Horizontal Merger Guidelines. These examples would provide merging parties with a "gold standard" to shoot for in their own analyses. Such a gold standard would increase the credibility of the Agencies in accepting and rejecting efficiencies claims. When claims are

[44] Muris, *supra* note 8. ("The dilemma is obvious – parties don't bother giving us good material, and without good material, we don't believe an efficiencies argument. It's the classic 'chicken and egg' problem.").

rejected, the gold standard examples would allow parties to understand how their analyses fell short. Most importantly, this benchmark would incentivize more effective analyses in the first place.

The examples would provide much-needed clarity on the amorphous concepts of merger specificity, verifiability, and cognizability. For example, does the merger specificity of an efficiency hinge on the demonstration that it is unachievable in *any* conceivable counterfactual, including those involving as-of-yet uncontemplated mergers or contracts? A literal reading of the Horizontal Merger Guidelines might support such a view, which would make the demonstration of merger specificity an all but insurmountable obstacle.[45] As I have argued elsewhere, I would condition merger review on what the market actually looks like, and not what the Agencies think it ought to look like.[46] A gold standard for merger specificity could usefully clarify that only those efficiencies that would be imminently realized by either independent firm should be discounted as not merger specific.

As a practical matter, these gold standard hypotheticals may resemble the 2006 Commentary on the Horizontal Merger Guidelines.[47] Of course, the gold standard approach need not preclude other types of guidance from the Agencies to the antitrust bar and the business community on efficiencies. I am eager to hear any ideas my fellow panelists may have about what types of Agency guidance would be most effective.

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[45] *See* Wright, *supra* note 37 ("For example, the merger-specificity requirement could be interpreted narrowly to exclude any efficiency that can be recreated with any form of creative contracting. While the Merger Guidelines assert that Agencies "do not insist upon a less restrictive alternative that is merely theoretical," there is little systematic evidence as to how this requirement is applied in practice.").

[46] Christine S. Wilson, *Reflections on the 2020 Draft Vertical Merger Guidelines and Comments from Stakeholders, Remarks at the DOJ Workshop on Draft Vertical Merger Guidelines*, at 9-10 (Mar. 11, 2020), https://www.ftc.gov/system/files/documents/public_statements/1568909/wilson_-_vertical_merger_workshop_speech_3-11-20.pdf.

[47] U.S. Dep't of Justice & Fed. Trade Comm'n, *Commentary on the Horizontal Merger Guidelines* (2006), https://www.ftc.gov/sites/default/files/attachments/merger-review/commentaryonthehorizontalmergerguidelinesmarch2006.pdf.

V. Case Studies

I now turn to three case studies that illustrate how various types of efficiencies have been analyzed in practice.

A. Arch/Triton

In May 2003, Arch Coal agreed to purchase Triton.[48] The deal would have combined Arch's two South Powder River Basin, or SPRB, coal mines with Triton's two SPRB mines. Arch announced in August 2003 that it would divest one of Triton's mines to a third party, who did not operate a mine in the river basin. At the time, four companies operating ten mines supplied most high-heat coal emanating from the basin. The transaction plus divestiture resulted in a modest increase in concentration, but no change to the number of firms producing SPRB coal. The FTC sued to block the transaction on the theory that it would increase the likelihood of coordination among the major coal producers in the basin. The District Court disagreed, and after the D.C. Circuit declined to stay the merger pending appeal, the FTC ended its attempt to block the merger.[49]

At trial, Arch claimed between $130 and $140 million in efficiencies that would be realized during the period from 2004 through 2008. The FTC appears to have dismissed these claims.[50] The district court was somewhat less skeptical, but concluded that "most – perhaps $100 million – of the purported savings from the acquisition […] have been called into question as either non-existent or overstated."[51] Instead, the court acknowledged that "some efficiencies

[48] A different transaction involving Arch Coal is currently in active litigation before the Commission. This document expresses no view on that matter.
[49] *FTC v. Arch Coal, Inc.*, 329 F. Supp. 2d 109, 153 (D.D.C. 2004).
[50] *Id.* at 71 ("Plaintiffs have systematically pointed out defendants' estimates of efficiencies and shown that defendants have not been able to quantify with precision the savings netted by the proposed transaction."). Neither the FTC's complaint nor its closing statement mentioned efficiencies.
[51] *Id.* at 75.

will naturally result from the transactions" and found that "[t]he realized efficiencies are more likely to be in the $35 to $50 million […] range."[52] Although the court found the FTC's *prima facie* case "far from compelling"[53] and concluded that it was unlikely that the transaction would substantially lessen competition, it stated that even $35 to $50 million in efficiencies could not "support a full defense based […] on efficiencies."[54]

The court rejected three claimed efficiencies as not being merger specific. Two related to Arch's planned recovery of coal at Triton's New Rochelle mine; in the court's view, an independent Triton was also likely to recover the coal. A third efficiency resulted from Arch's claim that its larger size would allow it to insure the Triton properties more cheaply than Triton could itself. The court rejected this argument, saying that "another potential purchaser of Triton might be able to achieve the same savings, and therefore they are not merger specific."[55]

The court also largely rejected a set of efficiency claims relating to increased utilization of equipment as being unverified. At trial, Arch presented estimates from an industry expert as evidence the savings would materialize. In the judge's view, the estimates were inadequately substantiated by quantitative studies or ordinary course documents.[56]

I applaud the *Arch* court's serious consideration of Arch's efficiency claims, but even in finding for the defendants it seems to treat merger harms and benefits asymmetrically. While acknowledging that the FTC's *prima facie* case was "weak," the court concluded that it *had* shown a *prima facie* case, largely based upon the structural presumption.[57] At the same time, the court rejected one efficiency claim because another – hypothetical – purchaser could have

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[52] *Id*. at 75 (emphasis in original).
[53] *Id.* at 84 (emphasis in original).
[54] *Id.* at 86.
[55] *Id.* at 73.
[56] *Id.* at 73-74 (describing claimed efficiencies relating to the elimination of duplicative repair parts; a tractor, drill grader, and loader; and three haul trucks).
[57] *Id.* at 84.

realized the same cost savings. It rejected other claims because they were insufficiently documented, despite the antitrust limitations on information sharing between merging rivals prior to consummation.

B. Edgewell/Harry's

In 2019, Edgewell, the maker of Schick razors, agreed to purchase Harry's, a startup that grew to prominence by offering low-priced razors directly to consumers through its website. The companies claimed the merger would result in productive efficiencies from transferring Edgewell product technology to Harry's razors, and marketing efficiencies from bringing Harry's marketing acumen to the Schick brand.[58]

In describing the marketing efficiency to the media, the companies relied on a qualitative argument. Since, the companies claimed, Harry's grew from nothing to a billion-dollar company on the strength of its brand and direct-to-consumer platform, it was natural to expect that the acquisition would result in improved branding and marketing of the struggling Schick brand.[59] As a general matter, there is little scope to substantiate this type of claim with hard numbers, detailed business plans, or ordinary course documents. Likewise, it is impossible for merging

[58] PR Newswire, *Edgewell Personal Care to Combine with Harry's, Inc. to Create a Next-Generation Consumer Products Platform* (May 9, 2019), https://ir.edgewell.com/news-and-events/press-releases/2019/05-09-2019-110141903?sc_lang=en ("The combined company will access Edgewell's exceptional product technology to continue building on Harry's shave and personal care products [. . .] Edgewell plans to capitalize on Harry's strength in brand positioning and design to enhance its North American Wet Shave offering to appeal to a broader and more diverse set of consumers."); Jim Cramer's interview with the CEOs of Edgewell and Harry's, https://www.youtube.com/watch?v=3iIRiIYb_Dc (in which Edgewell CEO Rod Little states "[w]e have great technology and IP around blades, we have global scale, infrastructure, and a great portfolio of well-established brands. On the Harry's side, they have digital marketing, brand building, design, a direct to consumer platform."),; Vox Recode interview with Jeff Raider, the CEO of Harry's, https://www.youtube.com/watch?v=bb8FNiTVkPE ("As a combined company, we think we'll be able to help drive growth for them in a more exciting way than we would as separate companies. You need amazing product technologies… and need brands that [people] are excited to want to buy. Between us, we have more robust capabilities in both areas than we would apart.").

[59] *See* Rani Molla, *Branding is the real reason Schick's parent company bought razor upstart Harry's for $1.4 billion*, VOX RECODE (September 9, 2019) (quoting Jeff Raider as saying Edgewell has "some iconic brands with lots of awareness and great products, but I don't think their brands always speak to the quality of their products"), https://www.vox.com/recode/2019/9/9/20857080/harrys-code-commerce-jeff-raider-edgewell.

companies to demonstrate that no other combination of firms or contractual arrangement would be capable of producing such benefits.

Does it follow that Agencies and courts should automatically discount qualitative claims like these as neither verifiable nor merger specific? My answer is "no." The Agencies should be neither credulous nor dismissive of such claims. Instead, they should treat them symmetrically with harm evidence, which, in my experience, is frequently qualitative. Weighing qualitative evidence of both harms and benefits is difficult, but within the Agencies' ability. This weighing is surely more principled than simply counting evidence on one side of the ledger and ignoring that on the other side.

Mergers can and do lead to the type of efficiency that Edgewell and Harry's aspired to, even when those kinds of efficiencies cannot reasonably be predicted *ex ante* in a manner that will satisfy the standards of the Horizontal Merger Guidelines. To take one example, in 1984 the FTC conditionally approved the GM-Toyota joint venture in part because it offered "a valuable opportunity for GM to complete its learning of more efficient Japanese manufacturing and management techniques."[60] Similarly, a recent paper by Professors Yonghong An and Wei Zhao finds that after the 1997 Boeing/McDonnell Douglas merger, prices for medium-sized wide body aircraft fell significantly.[61] In the authors' view, the price drop plausibly was attributable to accelerated "learning-by-doing" that resulted from the merger.[62] The authors catalog a literature

[60] *Statement of James C. Miller III, Chairman, Federal Trade Commission, Concerning GM/Toyota Joint Venture*, https://www.ftc.gov/sites/default/files/documents/commission_decision_volumes/volume-103/ftc_volume_decision_103_january_-_june_1984pages_374-497.pdf.

[61] Yonghong An & Wei Zhao, *Dynamic efficiencies of the 1997 Boeing-McDonnell Douglas merger*, 50 RAND J. ECON. 666 (2019).

[62] *Id.* at 688 ("These results indicate that even though there is no one-time experience transfer, the efficiencies from the accelerated learning-by-doing after the merger were still large enough to offset the effects of increased market power.").

finding similar effects in other industries.[63] Had these mergers been blocked because their efficiencies were discounted, consumers today would be worse off.

C. Alpha/Beta (masked FTC matter)

Two competing companies, Alpha and Beta, proposed to merge. The parties claimed the merger would lower their costs in three ways. First, the parties stated they would be able to consolidate all Atlantis production into Alpha's plant, and all Pangea production into Beta's plant, reducing shipping costs and fees paid to third-party logistics providers. Second, the parties expected to realize purchasing efficiencies, both by using the lower-cost source for each of various components and by obtaining volume discounts. Finally, Alpha planned to eliminate roughly forty percent of Beta's workforce.

The parties projected that efficiencies would reduce the combined firm's costs by roughly nine percent, based on a consultant's estimate prepared as part of Alpha's due diligence in evaluating Beta for purchase. The consultant had access to both parties' information and conditioned its projections on an algorithm which incorporated assumptions provided by Alpha. The consultant delivered its findings to Alpha in the form of a report. While Alpha shared the report with FTC staff, it shared neither the consultant's algorithm underlying the report nor justifications for the assumptions on which the algorithm was constructed. Consequently, FTC staff did not feel the consultant's report was an adequate basis for assessing the magnitude of these efficiencies. Moreover, Alpha and Beta had invested few resources into integration planning, and were unable to persuade FTC staff that any such planning had vindicated the consultant's algorithm.

[63] *Id.* at 668.

To take one specific example, the consultant's report concluded that Alpha could eliminate 84 percent of Beta's back office workforce, including Beta's entire IT department. The report did not explain how it arrived at this number, and Alpha did not provide any additional substantiation. In another example, the parties projected savings on logistics from reducing outsourcing, but provided little documentation on the cost of outsourcing relative to in-house logistics. They likewise declined to provide information on available capacity of in-house warehouses and trucks.

FTC staff thought it likely that the merger would lead to the types of efficiencies identified in the consultant's report. However, they found the consultant's report to be conclusory, and Alpha and Beta did not engage with FTC staff either to explain the methodology of the consultant's report or to provide ordinary course documents and data that would substantiate the report. Consequently, FTC staff viewed the efficiencies claims as lacking. While the consultant's report may have been useful for Alpha's due diligence, it was viewed by staff as inadequate to establish possible merger efficiencies as cognizable. When feasible, merging parties should hire an efficiencies expert to work in a clean room.

VI. Conclusion

Procter & Gamble's observation that "[p]ossible economies cannot be used as a defense to illegality" is the Supreme Court's latest statement on merger efficiencies.[64] Although it is unlikely that the language continues to reflect the Court's views, it has been instrumental in enabling lower courts and the Agencies to minimize efficiencies, or even to deem them irrelevant.[65] However, Justice John Harlan's concurrence in *Procter & Gamble* has perhaps

[64] *Procter & Gamble*, *supra* note 12.
[65] *See, e.g.*, *U.S. v. Anthem, Inc.*, 855 F. 3d 345, 355 (D.C. Cir. 2017) ("These very recent decisions put to rest the dissent's notion that 'no modern court' recognizes the continued viability of Procter & Gamble, see Penn State Hershey Med. Ctr., 838 F.3d at 348; Saint Alphonsus Med. Ctr., 778 F.3d at 789, while even a cursory reading of

proven even more durable. Harlan appears to strike a moderate tone in noting that the FTC "correctly[] seemed to accept the idea that economies could be used to defend a merger,"[66] even if they are advertising efficiencies, which the majority decision seemed to view as a harm. But in resolving the tension between the merger's apparent efficiencies and anticompetitive effects, Harlan provided a template for generations of jurists, stating that "I do not think, however, that on the record presented Procter has shown any true efficiencies in advertising."[67] In other words, plaintiffs and courts can reject efficiencies by saying they do not meet some amorphous standard, rather than having to weigh efficiencies and harms.

Improving on this treatment of efficiencies is not an insuperable problem. The Agencies should treat harms and efficiencies symmetrically, as they often claim to do.[68] Further, they should establish clear and reasonable expectations for what types of efficiency analysis will and will not pass muster. Doing so will incentivize merging parties to make the necessary investments in preparing analyses and will enable the Agencies to more credibly referee efficiency claims.

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the court's opinion today puts to rest any suggestion that it 'espouses the old . . . position that efficiencies might be reason to condemn a merger.'").

[66] Cf. Justice Harlan's concurrence at 603.

[67] *Id.*

[68] *See Statement of the Federal Trade Commission In the Matter of Ardagh Group S.A., Saint-Gobain Containers, Inc., and Compagnie de Saint-Gobain, April 11, 2014.*