SCHEDULED FOR ORAL ARGUMENT FEBRUARY 12, 2001

IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 00-5362

FEDERAL TRADE COMMISSION,
Plaintiff-Appellant,

vs.

H.J. HEINZ COMPANY, *et al.*,
Defendants-Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

BRIEF FOR PLAINTIFF-APPELLANT FEDERAL TRADE COMMISSION
PUBLIC COPY – SEALED MATERIAL DELETED

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November 29, 2000

CERTIFICATE AS TO PARTIES, RULINGS AND RELATED CASES

(A) Parties and Amici. All parties, intervenors and amici appearing before the district court and this Court are listed as follows:

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(B) Rulings Under Review. References to the rulings at issue in the present appeal are as follows:

FTC v. H.J. Heinz, Co., No. 00CV01688 (JR) (D.D.C. Oct. 18, 2000) (Robertson, J.) (Order Denying Plaintiff-Appellant's Motion for Preliminary Injunction).

(C) Related Cases. This case has not previously been before this Court and there are no related cases pending in this or any other court.

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GLOSSARY

1. Op. – District Court Opinion of October 18, 2000, denying preliminary injunction.

2. Mem. Op. – November 8, 2000, Memorandum of this Court granting injunction pending appeal.

3. Record Citations:

   Tr. – trial transcript.

   PX – plaintiff's exhibit.

   DX – Defendants' exhibit.

   App. – Joint Appendix

   SApp. – Supplement to Joint Appendix.

4. SKU – stock keeping unit.

STATEMENT OF JURISDICTION

This is an appeal from the denial of a statutory preliminary injunction that the Federal Trade Commission ("Commission") sought under Section 13(b) of the Federal Trade Commission Act, 15 U.S.C. § 53(b), in aid of an administrative proceeding to determine the legality of defendants' transaction under Section 7 of the Clayton Act, 15 U.S.C. § 18. The district court had jurisdiction under Section 13(b). Pertinent portions of Sections 7 and 13(b) are set out in the addendum attached to this brief.

This Court has jurisdiction over this appeal under 28 U.S.C. §§ 1291 and 1292(a)(1). The order under review denied all relief sought by the Commission in the district court and resolved all issues before that court. The order is also reviewable as an order refusing to grant an injunction. The order appealed from was entered on October 18, 2000, and the Commission filed its notice of appeal on October 19, 2000.

ISSUES PRESENTED

1. Whether the district court erred in denying the Commission a preliminary injunction in aid of an administrative proceeding pursuant to Section 13(b) of the FTC Act.
2. Whether the district court erred in crediting defendants' efficiencies defense.
3. Whether the district court properly weighed the equities in denying the preliminary injunction.

STATEMENT OF CASE; STATEMENT OF FACTS

A. Background

For over 60 years, Heinz, Beech-Nut, and Gerber[1] have dominated the prepared baby food market in the United States, described by Heinz as the most "lucrative world market" (PX 188 at 300; App. 2144) and by Beech-Nut as "oligopolistic." PX 39 at 547; App. 1777. Most supermarkets stock only two brands of baby food. Gerber, the market leader, is almost "invariably" one of the two brands, and Beech-Nut and Heinz compete head-to-head to be the second brand. Op. 5; App. 1420.

Heinz and Beech-Nut are locked in a "bidding and promotion war." PX 205 at 80; App. 2184. Heinz fights "for survival against Beech-Nut" (PX 397 at 061; App. 2680), and decries "aggressive Beech-Nut attacks at several accounts which have carried a high price tag." PX 140 at 38; App. 2072.

Beech-Nut's recent and substantial market share gains led Heinz's CEO, William Johnson, to ask, "What is Beech-Nut doing to drive share and fix their business?" Mr. Johnson expressed concern: "We need to keep our eye on this

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[1] "Heinz" refers to H.J. Heinz Co. "Beech-Nut" refers to Beech-Nut Nutrition Co., a subsidiary of Milnot Holding Co. ("Milnot"). "Gerber" refers to Gerber Products Co.

situation or we may well find ourselves in the number three position." PX 205 at 081; App. 2185. "To win [the fight for survival]," Heinz initiated plans to "develop and sell a comprehensive program focused on the customer and the consumer." PX 397 at 061; App. 2680. It responded to Beech-Nut's competition through "supplemental consumer initiatives" such as direct-to-consumer coupons (PX 431; PX 335; PX 801; PX 234 at 85; App. 2707-08, 2518-23, 2192), substantial increases in trade spending (PX 301 at 42; App. 2367), and increased attention to development of new products and packaging. *See* PX 205 at 080; App. 2184.

But rather than continue to "make the case" against Beech-Nut through price and innovation competition, Heinz chose another option: "acquire Beech-Nut if available, and merge the # 2 players." *Id.* In late 1999, Heinz approached Beech-Nut with a buy-out offer, which Beech-Nut accepted in February 2000. PX 698 at 19; App. 3760.[2]

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[2] At that time, Beech-Nut's CEO described the Beech-Nut division's recent marketing success as "remarkable – we'll do *********** in earnings this year on Beech-Nut alone!" PX 313 at 9010; App. 2507.

B. Statement Of The Case

The Commission filed this action seeking a preliminary injunction under Section 13(b) of the FTC Act in aid of an administrative proceeding challenging the merger. The Commission's complaint alleged that Heinz and Beech-Nut manufacture and sell baby food and that their merger would substantially lessen competition throughout the United States and in various local markets in violation of Section 7 of the Clayton Act. After brief expedited discovery, the district court held an evidentiary hearing. The court entered a decision and order denying a preliminary injunction on October 18, 2000. App. 1414.

The Commission sought an injunction pending appeal from the district court the next day. Upon denial of its application (App. 1463), the Commission sought emergency relief from this Court. On November 8, 2000, this Court issued an order and memorandum finding the Commission had demonstrated a substantial likelihood of success in this appeal and granting an injunction pending appeal. App. 1471.

C. Statement of Facts And Proceedings Below

1. The Parties

Heinz is the world's largest baby food company, with approximately $1 billion in sales worldwide. PX 336 at 577; App. 5619. It manufactures its jarred baby food for United States sales at its Pittsburgh, Pennsylvania plant. Op. 2;

App. 1417. Its baby food line includes about 130 SKUs (stock keeping units) PX 509 at 561; Tr. 683; App. 2932, 767.[3] Heinz's share of the United States jarred baby food market is approximately 17.4%. Op. 2; App. 1417.

Beech-Nut's baby food line consists of 128 SKUs. PX 310 at 3; App. 2490. Beech-Nut manufactures its jarred baby food at its facility in Canojaharie, New York. Milnot Admission ¶ 13; App. 1535. Beech-Nut's share of sales of jarred baby food in the United States is approximately 15.4% and its baby food business is profitable. Op. 2, 26 n.9; App. 1417, 1441.

2. The Product Market And The Baby Food Industry

There is no dispute that the manufacture and sale of jarred baby food constitutes a relevant line of commerce for antitrust analysis. Op. 10; App. 1425. Four million infants and toddlers consume prepared baby food in the United States. Total domestic sales of baby food are approximately $865 million to $1 billion. *Id.* at 2; App. 1417. Gerber is the largest domestic manufacturer of jarred baby foods, with a market share of 65%. *Id.* Gerber tends to have the highest shelf price (PX

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[3] Heinz's baby food business is profitable. PX 141 at 065; App. 2075; *see* PX 169 at 818; App. 2098. Baby food *********************************
*** in the Heinz USA Product Portfolio. PX 385 at 768; App. 2595.

304 at ¶ 25; App. 2377) and "is generally the first company to increase its price." Op. 4; App. 1419.

The district court found that Beech-Nut is generally perceived as close or equal in quality to Gerber and is close in shelf price. Heinz is perceived to be a somewhat lower quality. Heinz baby foods are marketed as the "value" brand, with a shelf price lower than Beech-Nut's and Gerber's in most areas of the country. *Id.* at 4-5; App. 1419-20. Regular users of each brand strongly prefer their brand over others. PX 98 at 627; App. 1967.

The focus of the Commission's case was the competition between Heinz and Beech-Nut at the wholesale level to be the second brand carried on retailers' shelves. Op. 12, 15; App. 1427, 1430. While at one time Beech-Nut and Heinz were regional companies, they increasingly overlap geographically. *See, e.g.,* PX 778; PX 1000; App. 3993-4000, 4278-81. This overlap flows from the continuing consolidation in grocery retailing, which is pushing supermarkets toward nationwide operation. A number of chains, including ****************************** that now operate either nationally or over large regions, prefer to stock the same brands in all their stores. *See, e.g.,* PX 816 at 18-19; App. 4257. Beech-Nut, for example, promotes itself to retail outlets nationwide as being a better quality and selling brand

than Heinz. PX 472 at 570 (switching from Heinz to Beech-Nut can help attract new shoppers and increase share of baby food market); PX 474 at 536; PX 477 at 80-84; PX 515 at 806-13; PX 516 at 95, PX 521; App. 2829, 2832, 2838-47, 2963-70, 2972, 2973-89.

Heinz and Beech-Nut also compete at the consumer, or retail, level through advertising, couponing, loyalty card discounts, product quality, innovations, shelf positioning, and product variety. *E.g.,* Tr. 208, 1146; App. 243, 1258. Beech-Nut currently spends about *********** annually on consumer spending activities. *See* PX 482 at 22-25 and Exhibit 2; PX 20 at 783-92; PX 92 at 924; PX 97 at 913-29; PX 472 at 543-44; PX 810 at 105; PX 813; App. 2877-78, 1746-55, 1919, 1941-56, 2827-28, 4250-51. Approximately ***** of Beech-Nut's most popular size baby food jars move through direct mail couponing. PX 344 at 340; App. 2551; *see* Tr. 912; App. 1023. Heinz also markets directly to consumers (PX 234 at 865; PX 431 at 80; PX 195; App. 2192, 2707, 2172-73), though generally Heinz does less couponing than Gerber or Beech-Nut. PX 694 at 160-61; App. 3576-77. Similarly, about ********** of Gerber volume is driven by direct mail coupons. PX 344 at 340; App. 2551.

3. The Geographic Markets

As the district court found, the relevant geographic market for wholesale competition is the United States. Op. 10; App. 1425. Both Heinz and Beech-Nut have substantial sales in all but a few local areas; and Gerber has distribution in all areas. PX 339 at 529; PX 63; PX 66 at 125, 128-30; PX 99 at 876; PX 426 at 001; App. 2532, 1829-33, 1870, 1873-75, 1995, 2706. There are no competitively significant imports of jarred baby foods into the United States. *See* PX 782 at ¶ 15; Tr. 218-19; PX 691 at 123; App. 4013, 253-54, 3534.

Retail markets are local from the consumer's perspective. Coupons are often distributed locally and can have a major impact. Tr. 219-20; PX 205; App. 254-55, 2183-85. Defendant's expert economist agrees that "retail competition takes place in localized (city-wide) markets." DX 617 at ¶ 17; App. 5220. Heinz and Beech-Nut closely track and target each other's sales and promotional activities in local markets (PX 17 at 429-44; PX 18 at 654-72; PX 3 at 553; PX 287 at 819; PX 56; PX 63 at 488-519; App. 1707-17, 1720-38, 1558, 2217, 1814-81, 1832-62), and Beech-Nut's average retail shelf prices tend to be lower in areas where Heinz is also distributed. PX 300 at 110; PX 20 at 757; PX 498 at 414; App. 2326, 1745, 2929. The district court noted that the Commission "has preserved its position that the proposed merger's effects may be evaluated at the regional or SMSA level," but

characterized the Commission's "advocacy of that position" as "perfunctory." Op. 10; App. 1425.

4. The Merger Would Significantly Increase Concentration In The Relevant Markets And Create A Duopoly.

The acquisition would create a nationwide duopoly for the manufacture and sale of jarred baby food in the United States. PX 782 at ¶ 22; Tr. 191-92; App. 4016, 223-25. The district court noted that the proposed merger would "increase the [Herfindahl-Hirschman ("HHI")] index to 5285, an increase of 510 points . . . five times the 100 point threshold established in the Merger Guidelines." Op. 11; App. 1426.[4] The court thus said: "[t]here is no serious dispute, and I find, that the proposed merger would increase concentration in an already highly concentrated market. That showing and my finding establish a prima facie case. . . ." *Id.* at 11-12; App. 1426-27.

It is also undisputed, although the district court made no finding on this point, that at retail there are at least ten metropolitan areas in which the HHI is above 1800 and the acquisition would increase the HHI by more than 500 points, giving the

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[4] The HHI, which is calculated by squaring the market shares of the market participants and then summing them, is used in the FTC and Department of Justice Antitrust Division Horizontal Merger Guidelines, 4 Trade Reg. Rep. (CCH) ¶ 13,104 at § 1.5 (1997) (App. 1485-86). Under the Guidelines, an industry is considered highly concentrated if the index exceeds 1800.

parties a combined market share exceeding 35%: Cleveland, Columbus, Cincinnati/Dayton, Roanoke, Raleigh/Greensboro, Charlotte, Atlanta, Jacksonville, Orlando, and Tampa/St. Petersburg. PX 781; App. 4003-04; *see also* DX 617 at App. B; DX 14 at 20; SApp. 5628-29, App. 4424.

5. Barriers To Entry

No significant competitor has entered the baby food market in nearly 60 years. On undisputed evidence (DX 617 at ¶ 26; Tr. 991-92; App. 5223, 1102-03), the district court found that high barriers made entry into the market "difficult and improbable." Op. 12; App. 1427.

6. Effects Of The Merger At Wholesale

Beech-Nut and Heinz are each other's most direct competitors for access to retail shelf space. Tr. 649; App. 731. Efforts by both firms to get on the shelf and stay there are at the heart of the competition between them. The competition is neither intermittent nor sporadic. Each explicitly recognizes the "constant threat" of the other. *See, e.g.*, PX 454 at 013, PX 311 at 266; App. 2739, 2503. Because this competition for shelf space is "all-or-nothing," it is especially intense. *E.g.*, Tr. 194-95, 1131-32; App. 228-29, 1243-44.

Wholesale accounts frequently switch between Beech-Nut and Heinz.[5] PX 316 at 614-15; App. 2514-15. Heinz thus reported that changes occurred in ****** ************* reviewed during its 1999 fiscal year (May 1998 to April 1999). PX 526 at 848; PX 199 at 688; App. 3007, 2181. In the Fall of 1999, Heinz identified ********************************** as an opportunity to increase Heinz's sales *************************. PX 526 at 848, 850; App. 3007, 3009.

Heinz and Beech-Nut aggressively compete against each other when submitting proposals to retailers.[6] These proposals involve numerous elements, including up-front dollars for stocking the product as well as various on-going payments and allowances. *E.g.,* PX 410 at 938; Tr. 584, 592; Heinz Admission

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[5] Competition for shelf space occurs not only as a consequence of mergers among supermarket chains, but also recurs periodically as retailers seek better deals from their suppliers. Tr. 146-47; DX 85 at 116-17; PX 306 at 108-09; Tr. 1130-31; App. 180-82, 4605-06, 2438-39, 1242-43. Heinz and Beech-Nut both monitor changes in the other's sales and distribution. *See, e.g.,* PX 406 at 283-85; PX 192 at 826-27; PX 4; Tr. 650 (Quinn, referring to PX 677); App. 2685-87, 2169-70, 1578-88, 734-35, 3209-10. Heinz specifically targets Beech-Nut distribution ** ** PX 339 at 535, 536; PX 394 at 679; Tr. 651; PX 118 at 434; App. 2534-35, 2676, 732-33, 2059.

[6] The proposed acquisition may have already led to reduced competition between Heinz and Beech-Nut. Beech-Nut has recently refrained from *********** *** PX 373 at 215; App. 2590.

¶ 26; App. 2700, 666, 674, 1531. These payments can affect the amount of shelf space allocated to the manufacturer's baby food products and number of SKUs placed on the grocer's shelves. Heinz Admission ¶ ¶ 32, 33; Tr. 1133-34; App. 1532, 1245-46. Heinz and Beech-Nut also make trade payments for displays that attract attention to the product. Such displays are especially beneficial to Heinz as a value brand. Tr. 621-22; App. 705-06.

Competition between Heinz and Beech-Nut at wholesale leads to innovation and other forms of nonprice competition. In its August 24, 1999, letter explaining its offer **************, Beech-Nut detailed some of its upcoming innovations: * ** *** **************************** PX 33 at 331; App. 1762. *See generally* PX 97 at 950-51 ("reinforce image that Beech Nut is the innovator in the area of infant feeding and nutrition"); Tr. 894, 1154 (Beech-Nut revolutionized baby food by taking out sugar, preservatives, and other unnecessary additives); App. 1957-58; 1005, 1266; PX 310 at 10; SApp. 5617.

Although Heinz characterized itself to the district court as a technology follower, rather than a leader (PX 421 at 341; PX 409 at 671; App. 2701, 2689), it

has focused on innovations that it believes could improve its competitive position against Beech-Nut. For example, Heinz has innovated as a means of gaining shelf space from Beech-Nut. *See, e.g.,* PX 366 at 845 ************************** PX 442 at 865 ** PX 420 at 292; SApp. 5620, 5623, 5621. And shortly before the onset of its merger discussions, Heinz had developed plans to "relaunch" the Heinz brand. PX 385; App. 2595-2606.

Thus, competition between Heinz and Beech-Nut at the wholesale level is robust and benefits wholesale customers. The district court acknowledged that "Heinz and Beech-Nut are competing and that a merger of the two companies will end that competition." Tr. 31; *see also* Op. 14-15; App. 1332, 1429-30. And this Court in granting the Commission an injunction pending appeal observed "it is indisputable that the merger will eliminate competition between the two merging parties at the wholesale level, where they are currently the only competitors for what the district court described as the 'second position on the supermarket shelves.'" Mem. Op. 1; App. 1472. Without discussing that evidence of lost wholesale competition, the trial court denied the preliminary injunction because it believed the

Commission had failed to show that wholesale competition has any "effect on shelf price." Op. 16-17; App. 1431-32.

7. Effects Of The Merger At The Consumer (Retail) Level

The record is replete with evidence showing that competition for shelf space not only has effects at the wholesale level, but also benefits the ultimate consumer. *E.g.,* PX 308 at 19-30; App. 2472-84. For example, after ******* received an unsolicited competing bid from ******************* (PX 687; PX 691 at 57; App. 3325-62, 3524), ***
***** PX 531 at ¶ 10; App. 3029. **
****
** PX 531 at ¶ 11; App. 3029.

Similarly, a senior executive from the Ahold supermarket chain testified that the payments resulting from Beech-Nut's winning bid enabled Ahold to offer its customers lower prices on baby food. Tr. 845-46; App. 956-57. The CEO of WinCo, another chain, also testified that ". . . all the moneys that we get from all of the vendors are basically for the same purpose . . . these moneys basically allow the public to buy groceries at a very, very low price including baby food." Tr. 143-44;

App. 177-78. Another chain *********** that carries Beech-Nut explained, ***
****
************************ PX 481 at ¶ 8; App. 2850.

Likewise, when competing at the wholesale level to convince supermarkets that its product will be the better choice for the second slot, each manufacturer engages in substantial direct-to-consumer promotion to increase share versus Gerber. *See* p. 9, *supra*. For instance, when Beech-Nut denigrated Heinz's direct-to-consumer discounting, Heinz immediately increased consumer discounts by $1.4 million. PX 177; App. 2123-24. After losing accounts to Beech-Nut, Heinz increased consumer spending. PX 367 at 006; App. 2577; *see also* PX 195 at 358-59; PX 335; PX 801; App. 2172-73, 2518-23, 4132.

The district court found that this sort of "trade spending does benefit consumers in theory," but concluded that the "record provides no basis for quantifying that benefit." Op. 16; App. 1431. The court also acknowledged that "[t]he FTC did submit examples of short-term couponing initiatives that resulted in lower prices." *Id.* at 17; App. 1432. Ultimately it concluded that, "absent a stronger connection between those couponing initiatives and competition between

Heinz and Beech-Nut for shelf space, *it is impossible to conclude with any certainty* that the consumer benefit from such couponing initiatives would be lost in the merger."[7] *Id.* (emphasis added).

8. Coordinated Interaction, Efficiencies, And Equities

Although this case presents a merger to duopoly, and although the court found that Heinz has "tended to follow Gerber prices" (Op. 4; App. 1419), it dismissed the Commission's central concern that, absent a third competitor, Gerber and Heinz are likely to engage in coordinated actions. It did so in a one-sentence footnote generally citing defendants' expert testimony of "structural market barriers" without explaining why these factors are dispositive. *Id.* at 20 n.7; App. 1435. The district court cited (*Id.* at 16-17; App. 1431-32), but did not otherwise discuss the extensive testimony by plaintiff's expert economist describing how Beech-Nut currently serves to disrupt Heinz and Gerber from engaging in coordinated interaction. *See, e.g.*, Tr. 197-99 (Hilke); PX 782 at ¶¶ 84-86; App. 231-33, 4041-43.

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[7] In contrast, this Court noted that the merger of Heinz and Beech-Nut "creates, by a wide margin, a presumption that the merger will lessen competition at the retail level." Mem. Op. 1; App. 1472.

There is also general agreement that the merger could conceivably yield *some* cost-savings to defendants, although the amount is only approximated in the record. Without analyzing them, the court found cost savings in a range between $9.4 - $12 million in a market that it valued at between $865 million to $1 billion. Op. 2, 21; App. 1417, 1436. The court also expressly declined to find that Heinz would use these cost savings "to mount vigorous competition against Gerber for shelf space and market share." *Id.* at 23; App. 1438. In approving the merger it relied on the "enhanced prospects of the merged entity to introduce innovative products" (*id.* at 20; App. 1435), although it is undisputed that the principal products Heinz "intends" to introduce are not yet commercially feasible in the United States, and may never be. Tr. 639-41, 646; PX 694 at 82-83; App. 721-23, 728, 3557.

As to the equities, the court found that the Commission's anticipated administrative review of the merger will be futile, absent an injunction, because Beech-Nut's manufacturing facility "will be closed," its "distribution channels will be closed, the new label and recipes will be in place, and it will be impossible as a practical matter to undo the transaction." Op. 27; App. 1442. Notwithstanding these obstacles to effective Commission review absent an injunction, the court denied an injunction because it perceived that defendants would terminate the transaction rather than pursue an appeal. *Id.* In contrast, this Court granted the

Commission an injunction pending appeal because "the public interest in enforcement of the antitrust laws is strong, any injury from going forward with the merger would plainly be irreversible, while the same cannot be said for any loss to competition from its delay." Mem. Op. 3; App. 1474.

SUMMARY OF ARGUMENT

The Commission seeks a preliminary injunction in aid of an administrative proceeding challenging a merger to duopoly. In the proceeding below, the Commission demonstrated that the proposed merger will substantially increase concentration in the already highly concentrated market for jarred baby food. It is undisputed that barriers to entry in that market are very high and that the parties are thriving businesses. The Commission thus clearly satisfied all the criteria for securing a preliminary injunction established under this Court's decision in *FTC v. PPG Indus., Inc.*, 798 F.2d 1500 (D.C. Cir. 1986). The district court erred in denying injunctive relief.

The district court also erred in analyzing the merger's effects on the wholesale and retail markets. While recognizing that the wholesale market was the primary focus of the Commission's case, the court denied a preliminary injunction because it found that the Commission failed to prove that wholesale competition results in quantifiable benefits to consumers at the *retail* level. Section 7, however,

does not require the government to show anticompetitive effects in downstream markets when it challenges a merger between parties that directly compete in an upstream market. The court acknowledged that the transaction would eliminate a substantial amount of competition at wholesale – that is plainly a substantial lessening of competition in a "line of commerce" that violates Section 7. An injunction should have issued on that basis alone.

The court's analysis of competitive effects in the consumer market is also fatally flawed. There, the court held that the Commission was not entitled to a preliminary injunction because the Commission's evidence was "inconclusive" and the court found it "impossible to conclude with any certainty" that the merger would harm consumers. However, an inability to "conclude with any certainty" is not even a proper standard after a full trial on the merits under Section 7, let alone in a preliminary injunction proceeding under Section 13(b). Under the correct standard, the Commission is also entitled to a preliminary injunction because of the merger's effects on retail competition.

Nor can the district court's decision be salvaged by the court's casual observation that coordinated action between Heinz and its sole competitor in the post-merger market is unlikely. No other court has ever allowed a merger to duopoly when there are high entry barriers and neither firm is failing, precisely

because the law and solid economic theory agree that two-firm markets are prone to collusive interaction. Moreover, the record here amply shows that the baby food market is so prone. In any event, a preliminary injunction is not the appropriate stage of the proceedings for the district court to determine – contrary to nearly 40 years of merger law under Section 7 – that collusion is unlikely in a two-firm market.

Defendants tried to overcome the Commission's right to a preliminary injunction by claiming that such significant efficiencies would result from the merger that the net result would be pro-competitive. The lower court erred in uncritically accepting defendants' efficiencies claims at the preliminary injunction stage of the case. Moreover, defendants failed to make the requisite showing here. Defendants' claims are highly speculative and, relative to the size of the market, so modest that they would be swamped by even a small anticompetitive price increase. Also, the claimed efficiencies are not cognizable because they depend on an anticompetitive reduction in consumer choice, can be achieved without combining defendants' jarred baby food businesses, and depend on the incorrect (and unproven) premise that this otherwise anticompetitive merger can be justified because it may enable the merged entity to compete better against Gerber. In any event, defendants' efficiencies claims need to be examined in a full trial on the merits.

Finally, the court erred in weighing the equities. Although it correctly recognized that, once consummated, the merger will not be undone and that the Commission's administrative proceeding would become a futile gesture, it nonetheless found that defendants' threat to abandon the transaction "tipped the balance" in favor of denying a preliminary injunction. This was grave error. Nothing in the record shows that defendants actually plan to abandon their transaction. Equally important, at the time defendants planned their merger, they were aware of the need for premerger review and it was certainly foreseeable that the government would take careful note of a merger to duopoly. Any failure by defendants to allocate sufficient time in their schedule for meaningful judicial and administrative review of their transaction is simply not an equity that outweighs the public interest in preserving competition.

ARGUMENT

The district court's rulings on matters of law are subject to plenary review by this Court. *Ambach v. Bell,* 686 F.2d 974, 979 (D.C. Cir. 1982). *Accord Ayuda, Inc. v. Thornburgh,* 948 F.2d 742, 757 (D.C. Cir. 1991); *Foltz v. U.S. News & World Report,* 760 F.2d 1300, 1306 (D.C. Cir. 1985).

This Court "do[es] not afford deference when the appeal presents a substantial argument that the trial court's decision was premised upon an erroneous

legal conclusion." *Ayuda,* 948 F.2d at 757, *citing Foundation on Economic Trends v. Heckler,* 756 F. 2d 143, 152 (D.C. Cir. 1985). "When the district court's estimate of the probability of success depends on an incorrect or mistakenly applied legal premise, 'the appellate court furthers the interest of justice by providing a ruling on the merits . . . .'" *Air Line Pilots Ass'n v. Eastern Air Lines, Inc.,* 863 F.2d 891, 895 (D.C. Cir. 1988).

Although the district court's factual findings are subject to review under the "clearly erroneous standard" (*e.g., PPG,* 798 F.2d at 1504), in several instances (likelihood of coordinated action, effects of the merger at the wholesale level and in local markets) it failed to make any factual determinations at all. When the court failed to "set forth the findings of fact," it did not satisfy its obligations under Fed.R.Civ.P. 52(a), which applies fully to preliminary injunction cases. *Mayo v. Lakeland Highlands Canning Co.*, 309 U.S. 310, 316 (1940) ("It is of the highest importance to a proper review of the action of a court in granting or refusing a preliminary injunction that there should be fair compliance with Rule 52(a) . . . "). This Court may therefore make its own assessment of whether the Commission has shown a likelihood of success in proving these aspects of its case. *See* 9 *Moore's Federal Practice 3d* § 52.12[2] ("If the appellate court can discern enough solid facts from the record as a whole to enable it to render a decision, it may proceed to

review the trial court order, despite the fact that the findings are themselves inadequate”).

I. The Commission Made The Showing Required By Section 13(b) of The FTC Act.

A. The Commission Satisfied The Criteria For A Preliminary Injunction.

The Commission sought a preliminary injunction pursuant to Section 13(b) of the FTC Act, which provides that the Commission is entitled to an injunction “[u]pon a proper showing that, weighing the equities and considering the Commission’s likelihood of ultimate success, such action would be in the public interest.” Several courts have held that this language means that the Commission is entitled to a preliminary injunction if it “raise[s] questions going to the merits so serious, substantial, difficult and doubtful as to make them fair ground for thorough investigation, study, deliberation and determination by the FTC in the first instance and ultimately by the Court of Appeals.” *FTC v. University Health,* 938 F.2d 1206, 1218 (11th Cir. 1991); *FTC v. Warner Communications,* 742 F.2d 1156, 1162 (9th Cir. 1984); *FTC v. Cardinal Health*, 12 F. Supp.2d 34, 44 (D.D.C. 1998); *FTC v. Staples,* 970 F. Supp. 1066, 1071 (D.D.C. 1997); *see also FTC v. Beatrice Foods, Inc.*, 587 F.2d 1225, 1229 (D.C. Cir. 1978). The Commission “need not prove that the proposed merger would in fact violate Section 7 of the Clayton Act,” a matter

"reserved for the FTC." *Cardinal Health*, 12 F. Supp.2d at 45. "Doubts are to be resolved against the transaction" and in favor of a preliminary injunction. *FTC v. Elders Grain, Inc.*, 868 F.2d 901, 906 (7th Cir. 1989) (Posner, J.).

The Commission satisfied all the criteria for obtaining a preliminary injunction in this case. It demonstrated, and the lower court found, that the merger will lead to further increases in concentration in a market that is already highly concentrated; that high barriers to entry in that market make it unlikely that any anticompetitive effects will readily be undone; and the acquired firm is in no danger of failing. Op. 11, 12, 26 n.9; App. 1426, 1427, 1441. As this Court (per Judge Bork) observed in *PPG* (a case with lower concentration than the present one):

> The pre-acquisition HHI calculated by the district court shows that the relevant market . . . is already "highly concentrated" and the effect of the acquisition would be a dramatic increase in concentration. . . . The district court also found high market-entry barriers that would prolong high market concentration. *There is no doubt that the pre- and post-acquisition HHI's and market shares found in this case entitle the Commission to some preliminary relief.*

798 F.2d at 1503 (emphasis added).

The district court here did not even cite *PPG*. Rather, it based its decision principally on *United States v. Baker Hughes, Inc.,* 908 F.2d 981 (D.C. Cir. 1990), a case that Heinz has suggested to this Court overruled *PPG*. *See* Heinz Opp. to FTC Motion for Injunction Pending Appeal 9 n.5. However, there is no conflict

between the two decisions,[8] and *Baker Hughes* does not support the district court's conclusion. In *Baker Hughes*, this Court sustained the denial of a permanent injunction after a full trial on the merits where the shares in the relevant market were "volatile and shifting" and "easily skewed" (*id.* at 986) and "entry was likely" (*id.* at 987). In those circumstances, high market shares were not an accurate predictor of future competition, and low entry barriers made it unlikely that the merged entity could ever exercise market power to harm competition. None of these factors is present in this case. Market shares are high and stable and high entry barriers will indefinitely, perhaps permanently, preserve a Heinz/Gerber duopoly.

Also, the two cases came to this Court in different procedural postures. *PPG* was an appeal in a preliminary injunction case, as is this case. *Baker Hughes* was an appeal after a trial on the merits. Thus, the two cases stand for two different propositions: *PPG* sets the standard for showing a likelihood of success on the merits. *Baker Hughes* sets the standard for succeeding on the merits.

As this Court held in *PPG,* there is a "presumption in favor of a preliminary injunction when the Commission establishes a strong likelihood of success on the merits." 798 F.2d at 1507. That is precisely what this Court found the Commission

[8] This Court, in its earlier Order and per curiam opinion in this proceeding, cited both cases, thus reaffirming the vitality of *PPG.*

has done in this case. Mem. Op. 1; App. 1472. This Court's decision in *PPG* thus compels the entry of preliminary relief so the Commission, and ultimately a reviewing court, can fully assess the competitive impact of defendants' proposed merger.

B. The Court Erred In Its Analysis Of Competitive Effects At The Wholesale And Retail Levels.

The district court correctly observed that "[t]he focus of the Commission's case is the competition between Heinz and Beech-Nut for the second position on the supermarket shelves. . . ", whereas the "other basic level of competition, labeled 'consumer competition' [] was addressed at length by defendants." Op. 12-13; App. 1427-28. We show below that the Commission proved its case at the wholesale level (the level specifically challenged in its complaint) and not only rebutted the retail case addressed by defendants, but also established a right to a preliminary injunction based on retail effects as well.

1. The Court Erred In Its Assessment Of The National Wholesale Market.

Competition between Heinz and Beech-Nut to gain accounts at the wholesale level is vigorous, constant, and intense. Because each contest between them has a winner-take-all result, the two firms are permanently locked in a struggle for their very survival. Heinz and Beech-Nut have never denied this. While agreeing "that

Heinz and Beech-Nut are competing and that a merger of the companies will end that competition" (Tr. 31 (closing argument); App. 1332), the lower court did not address the intense bidding war between the parties at the wholesale level, as if that competition were a matter of no consequence. Instead, the court found that the Commission was not entitled to a preliminary injunction because it had not adequately shown that wholesale competition benefits retail consumers. Op. 12-13; App. 1427-28. The court thus determined that competition at the wholesale level is relevant only if directly and quantifiably linked to prices at the retail level. *Id.* at 11-15; App. 1426-30. This was clear legal error.

Section 7 applies to "*any* line of commerce" and does not require the government to show the retail price effects of a merger that lessens competition at the manufacturing or wholesale distribution level. And for good reason. There are thousands of intermediate goods markets (ranging from chemicals and electrical components to large and complex machines) that could be virtually immune from Section 7 analysis if the government had to show anticompetitive effects not just in those markets, but in downstream markets as well.

For example, when an automobile manufacturer obtains a better price on tires through a competitive bid, it may not be possible to trace the dollar savings to retail automobile prices. Yet, Section 7 presumes that competition is beneficial, whether

the effects are quantifiable or not. The law does not, and should not, permit mergers to monopoly or duopoly in industries that provide parts that are incorporated into larger products that are then sold to consumers merely because the government is unable precisely to trace the savings pocketed by firms or passed on to consumers in every subsequent intermediate or final goods market.[9]

The district court's holding, requiring a Section 7 plaintiff to prove anticompetitive effects in downstream consumer markets, is contrary to every other case of which we are aware that has involved attempted mergers between competitors in upstream levels of commerce. For example, in *PPG*, this Court directed the district court to enjoin a proposed merger between manufacturers of aircraft transparencies (canopies) engaged in design and bid competition to supply aircraft manufacturers. In doing so, this Court did not demand proof that

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[9] In another context, the Supreme Court has found that such a burden would be enormous because of the "uncertainties and difficulties in analyzing price and output decisions" in multi-level industries. *See Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977). There, the Court held that these difficulties require a prophylactic rule relieving direct purchasers from showing how (or even whether) anticompetitive overcharges are "passed on." At the same time, the Court also limited damage actions to such direct purchasers. Under *Illinois Brick*'s principles, the district court should not have required the Commission to prove pass-through to ultimate consumers under Section 7 – an incipiency statute that is satisfied "where in *any line of commerce* or in *any activity affecting commerce* in any section of the country, the effect of such acquisition *may be* substantially to lessen competition, or *tend to* create a monopoly." 15 U.S.C. § 18 (emphasis added).

competition between the two firms ultimately affected either the price of aircraft or the price of commercial airline tickets. Rather, once this Court found evidence that the firms bid against each other, the nature of that competition did "not merit further discussion." 798 F.2d at 1505. Likewise, in *United States v. El Paso Natural Gas Co.,* 376 U.S. 651 (1964), the Supreme Court recognized that even unsuccessful bidders can have significant influence on the pricing and other business strategies of competing wholesale suppliers; but the Court did not require proof that competition at the upstream level ultimately benefits consumers. In both cases, the transactions were enjoined because they were likely substantially to lessen competition at the wholesale level.

Similarly, in *Elders Grain, supra,* the Seventh Circuit affirmed an injunction against two merging grain mills without requiring that the Commission show an effect on consumer prices for cereals and other corn products. And in *Cardinal Health, supra,* the district court enjoined two mergers between wholesale pharmaceutical distributors even though there was no showing that consumers would have to pay higher retail drug prices.

Here, the Commission introduced unrebutted evidence of competition between Heinz and Beech-Nut for wholesale accounts. Such competition plainly resulted in lower effective prices to supermarkets. *See, e.g.,* PX 205; App. 2183-85.

The district court thus erred legally in analyzing the loss of wholesale competition and in demanding that the Commission quantify the benefits of that competition to downstream retail consumers.

2. The Lower Court Applied The Wrong Standard To Local Retail Markets.

In approaching retail markets as it did, the lower court imposed upon the Commission an inappropriate burden of proof. While characterizing the Commission's showing regarding local markets as "perfunctory" (Op. 10; App. 1425), the court acknowledged that "[t]he FTC did submit examples of short-term couponing initiatives that resulted in lower prices." *Id*. at 2; App. 1417. Overall, however, the court found the Commission's evidence "inconclusive," and ultimately found that "it is impossible to conclude with any certainty that the consumer benefit from such couponing initiatives would be lost in the merger."[10] *Id*. at 17; App.

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[10] The district court also acknowledged that "variable" trade allowances by the defendants directly benefit consumers "in theory", but concluded that wholesale competition primarily increased "fixed" spending and that such competition produced no consumer benefits. Op. 15-16; App. 1430-31. In so holding, the court ignored testimony that even truly fixed payments lead to consumer benefits (PX 691 at 64-65, 111-12, 130-31; Tr. 143-44, 547, 551, 845-46; App. 3526, 3532, 3535, 177-78, 629, 631, 955-57) and disregarded the fundamental premise of Section 7, which is that all competition is ultimately beneficial, regardless of whether the effects are predictable with certainty (*see* p. 32, *infra*). But even if the court's (clearly erroneous) finding is accepted, its import is to strengthen the Commission's showing discussed in the preceding section of this brief, *i.e.*, the merger harms

1432. However, the inability of a trial court "to conclude with any certainty" is not an appropriate standard for withholding relief under Section 7, and it is an especially inappropriate standard for withholding preliminary relief under Section 13(b) of the FTC Act.

To establish a violation, the Commission need show only a reasonable probability, not a certainty, that anticompetitive activity may occur. "All that is necessary is that the merger create an appreciable danger of [anticompetitive] consequences in the future." *Hospital Corp. of America*, 807 F.2d at 1389 (Posner, J.). Thus, Section 7 "creates a relatively expansive definition of antitrust liability," by requiring a showing that the merger's effect "*may be* substantially to lessen competition." *California v. American Stores Co.*, 495 U.S. 271, 284 (1990) (emphasis in original). The statute does not even require a high probability that a merger will substantially lessen competition. *Elders Grain,* 868 at 906.

If the evidence relating to the consumer (retail) market is viewed under proper Section 13(b) and Section 7 standards, the Commission's right to a preliminary injunction is clear. Although Heinz and Beech-Nut rarely appear on the same retail

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wholesale competition. Even if fixed allowances are simply pocketed by retailers, any diminution of those allowances occasioned by Heinz's no longer having to vie for the second slot on the shelf effectively raises the cost of baby food at the wholesale level.

shelf, they compete from different stores within local markets.[11] *See, e.g.,* Tr. 147-48, 172; PX 531 at ¶ 8; PX 481 at ¶ 12; PX 479 at ¶¶ 6-7; PX 478 at ¶ 6; App. 181-82, 206, 3028-29, 2851-52, 2845, 2843. There are at least ten metropolitan areas in which both firms have more than 10% of the market and their combined share would exceed 35%. PX 781 at Ex. 1B; App. 4003-04; *see also* DX 617 at App. B; SApp. 5628-29; PX 18 at 656-73; PX 38 at 800-01; DX 14 at 20; DX 276; App. 1722-39, 1774-75, 4424, 4733. As this Court observed, the high market concentration in this case "creates, by a wide margin, a presumption that the merger will lessen competition at the retail level." Mem Op. 1; App. 1472.

Moreover, Gerber's market share is lower in markets where both Heinz and Beech-Nut are significant factors than when it faces significant competition from only Heinz or Beech-Nut. Tr. 224, 246, 1150; PX 782 at ¶ 24; PX 781; PX 711;

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[11] Defendants' expert reached a contrary opinion through an econometric analysis. Tr. 998; App. 1109. However, his analysis was fundamentally flawed because it effectively "proves" that Heinz and Beech-Nut baby food are not even in the same product market. Tr. 1030-1032; App. 1141-43. The analysis is therefore not entitled to any weight. *See, e.g., Smith v. Virginia Commonwealth University*, 84 F.3d 672 (4th Cir. 1996) (omission of major variables from regression model raised material question of fact as to validity of the study and required reversal of grant of summary judgment)*; Polaroid Corp. v. Eastman Kodak Co.,* 16 U.S.P.Q.2d 1481, 1990 WL 324105 (D. Mass. 1990) (econometric analysis that is inconsistent with contemporaneous business documents and the testimony of knowledgeable fact witnesses should be highly suspect).

App. 259, 281, 1262, 4017, 4003-04, 3843. Beech-Nut retail shelf prices also are lower in the so-called "mixed" markets, where Beech-Nut is competing to some degree to be the "value brand." Tr. 247-48; App. 282-83.[12]

Given that the merger will substantially increase concentration in major local retail markets that are already highly concentrated, that barriers to entry are high, and the evidence showing that Heinz and Beech-Nut compete through couponing initiatives and by other means for the pocketbooks of retail consumers in those markets, the Commission established a reasonable probability, if not a certainty, of likely anticompetitive effects at the retail level. That loss of retail competition provides – even apart from the dramatic loss of competition at the wholesale level – ample basis for a preliminary injunction.

C. The District Court Erred In Finding There Is No Likelihood Of Collusion Or Coordinated Action In A Post-Merger Market Consisting Solely Of Heinz And Gerber.

As shown in the preceding section, the district court gravely erred in failing to recognize the direct loss of competition that the proposed merger will engender at

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[12] *See* DX 14 at 20 ** ** ******************** App. 4424; *see also* PX 174 at 026; PX 20 at 757; PX 95 at 681; App. 2122, 1745, 1922.

both levels: the immediate loss of vigorous, head-to-head competition at the wholesale level to be the number two brand on retailers' shelves, and the equally immediate loss of consumer benefits in those local retail markets where three-way competition has lowered prices.

The court below seriously compounded its error, moreover, by dismissing one of the key concerns in any horizontal merger case, which takes on dramatic relevance in this merger-to-duopoly context: the prospect that the remaining firms will engage in either collusive or tacitly coordinated behavior, thus lessening competition on a continuing basis. As this Court has held, "[w]here rivals are few, firms will be able to coordinate their behavior, either by overt collusion or implicit understanding, in order to restrict output and achieve profits above competitive levels." *PPG*, 798 F.2d at 1503.

It is settled law that "significant market concentration makes it 'easier for firms in the market to collude, expressly or tacitly, and thereby force price above or farther above the competitive level.'" *University Health*, 938 F.2d at 1218 n.24. As the Supreme Court has observed, as concentration increases the "greater is the likelihood that parallel policies of mutual advantage not competition will emerge." *United States v. Aluminum Co. of America*, 377 U.S. 271, 280 (1964). The threat is that "firms in a concentrated market might in effect share monopoly power, setting

their prices at a profit-maximizing, supracompetitive level by recognizing their shared economic interests and their interdependence with respect to price and output decisions."[13] *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 227 (1993).

A merger is illegal under Section 7 if the remaining firms will be more likely to engage in conduct that may result in higher prices, even if that conduct, in itself, would be lawful.[14] This merger raises the very competitive problem – a tightening of oligopoly market conditions – that lies at the heart of Section 7. Such coordination:

> is feared by antitrust policy even more than express collusion, for tacit coordination, even when observed, cannot easily be controlled directly by the antitrust laws. It is a central object of merger policy to obstruct the creation or reinforcement by merger of such oligopolistic market structures in which tacit coordination can occur.

Antitrust Law, ¶ 901b2 at 9; *see University Health*, 938 F.2d at 1219 (four firms "easily could collude to [raise prices or reduce output] without committing detectable violations of . . . the Sherman Act").

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[13] Defendants' expert economist testified to the same effect. Tr. 1106-07; App. 1218-19.

[14] Section 7 "is concerned with far more than 'collusion' in the sense of an illegal conspiracy; it is very much concerned with 'collusion' in the sense of tacit coordination not amounting to conspiracy." Phillip Areeda, IV Antitrust Law ¶ 916, at 85 (rev. ed. 1998) ("Antitrust Law"); *see Merger Guidelines*, § 2.1.

The Commission provided overwhelming evidence that the merger will bring about or exacerbate the very market conditions – high concentration levels, barriers to entry, reduced excess production capacity, increased product homogeneity, elimination of all-or-nothing competition for the second position on the shelf, an industry history of coordinated interaction – that increased the likelihood of coordinated interaction. In a single sentence in a footnote the district court found that evidence "effectively rebutted by Dr. Baker's testimony regarding the structural market barriers to collusion in the market. *See* Tr. 1010-23." Op. 20 n.7; App. 1435. The court cited no law on the point.[15]

The strong presumption under *PPG* that the Commission is entitled to a preliminary injunction in circumstances such as those found here cannot be overcome by the district court's casual observation. The notion that collusion is unlikely in a market with only two players is contrary to all known precedent.[16] It is also inconsistent with the lower court's observations that Heinz generally follows

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[15] *See Knapp Shoes, Inc. v. Sylvania Shoe Mfg. Corp.*, 15 F.3d 1222, 1227-29 (1st Cir. 1994) (single sentence in footnote not sufficient explanation of basis for ruling under F.R.C.P. 52(a)).

[16] As this Court observed in granting the Commission an injunction pending appeal in this case: "[a]s far as we can determine, no court has ever approved a merger to duopoly under similar circumstances." Mem. Op. 2; App. 1473.

Gerber's pricing lead (Op. 4; App. 1419)[17] and that both Heinz and Beech-Nut have retreated from previous competitive efforts in response to competitive pressure from Gerber. *Id.* at 17-19, 23 n.8; App. 1432-34, 1438. Evidence that price leadership is already occurring with three market participants supports the common-sense conclusion that reducing the market to two players will make the situation worse. Moreover, while the court suggested that "structural antitrust doctrine" has limited value (*id.* at 19; App. 1434), the experience of this Court, and others as well, is that structure and concentration are good predictors of post-merger effects. *E.g., PPG,* 798 F.2d at 1503; *University Health*, 938 F.2d at 1219-20; *Elders Grain,* 868 F.2d at 905-06 (barring acquisition that increased market share of largest firm from 23% to 32%); *California v. American Stores Co.,* 872 F.2d 837, 842 (9th Cir. 1989), *rev'd on other grounds*, 495 U.S. 271 (1990); *Warner Communications,* 742 F.2d

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[17] Over the last two years, Gerber has raised list prices twice and Heinz has followed. *See* Tr. 503-04; App. 587-88. Beech-Nut ************************ *** *E.g.,* DX 408 at 900 ******; App. 4872. If anything, the merger will improve Heinz's ability to follow Gerber prices. Moreover, as defendants' expert has noted, with today's improving information technologies, firms "are increasingly able to observe prices and quantities sold on a weekly, daily, hourly, and even transaction-by-transaction basis." Baker, "Contemporary Empirical Merger Analysis," 5:3 George Mason L. Rev. 347, 348 (1997).

at 1163 (barring acquisition that increased market share of second largest firm from 19% to 26%). These cases cannot be so easily ignored, particularly in the case of a preliminary injunction seeking to preserve the status quo so a full record can be developed.

At this stage, nothing in the record undercuts the presumption that the merger will lessen competition and facilitate coordinated interaction between Heinz and Gerber. Under current conditions, any effort by Heinz and Gerber to coordinate pricing and marketing policies would be frustrated because Beech-Nut's very existence as an independent competitor foils any such efforts. Tr. 197-99; PX 782 at ¶¶ 84-86; App. 231-33, 4041-43. Heinz cannot assure Gerber that it will not have to drop prices (increase discounts and allowances) to keep Beech-Nut from taking the second slot. This competitive Beech-Nut presence increases the other firms' uncertainty in reaching an agreement, and opens a plausible excuse for Heinz to cheat. Both problems reduce the prospects of successful coordinated interaction. Tr. 197-99; App. 231-33. Thus, competition between Beech-Nut and Heinz is "the linchpin that keeps the market honest." Tr. 282; App. 317. But a reduction in the number of firms from three to two would leave two firms competing for two slots; this is like a game of musical chairs where there are two chairs and two players – in other words, not much competition. Tr. 260; App. 295.

A number of other factors will increase the likelihood of coordination from this merger. Currently, Heinz, Beech-Nut, and Gerber have very different image-cost characteristics: Gerber is a premium product with low cost of production; Beech-Nut is a premium product with higher production cost; and Heinz is a value product with lower production cost (*see* Op. 4-5; App. 1419-20); Heinz and Beech-Nut have differing market shares across the country; both have excess capacity; and there is significant winner-take-all competition between them. PX 308 at 3-19; PX 304 at ¶¶ 22-26, 37-38, 50-52, 61; App. 2456-72, 2376-78, 2382-83, 2387, 2390.

Post-merger, Heinz and Gerber quality and costs would be closer, excess capacity would be reduced, if not eliminated, and the disruptive influence of the winner-take-all competition between Beech-Nut and Heinz would evaporate.[18] PX

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[18] Firms that that compete against each other regularly in the marketplace have a great incentive to co-operate. In these "repeat game" situations:

> The cost of cheating is that the cheater will never receive the cartel price in the future; burned once, the cheater's rivals will never agree to the cartel price again. So each firm sees the following choice. It can cheat one time, then forever compete. Or, it can never cheat, [and] earn the cartel price forever. Unless the firm cares very little about future profits, . . .[i]t will never cheat on the cartel price.

Baker, "Two Sherman Act Section One Dilemmas: Parallel Pricing, the Oligopoly Problem, and Contemporary Economic Theory," 38 Antitrust Bulletin 143, 154-55 (Spring 1993).

782 at ¶¶ 78-90; App. 4039-44. With only two firms remaining, monitoring a coordinated agreement will be easier. *See United States v. Ivaco*, 704 F. Supp. 1409, 1428 n.18 (W.D. Mich. 1989). Moreover, the mere fact that Heinz and Gerber products differ slightly does not diminish their ability to collude or otherwise engage in coordinated action:

> In general, coordinating firms might reach a consensus by establishing as focal (self-evident) one or more simple and readily grasped behavioral rules. For example, the firms might preserve existing price differentials across product types and brands, and preserve existing percentage discounts to wholesalers or retailers, while merely altering the entire structure of pricing by a common percentage.

Baker, "Predatory Pricing After Brooke Group: An Economic Perspective," 62 Antitrust L.J. 585, 600 n.74 (1994); *see Hospital Corp. of America*, 807 F.2d at 1390 (rejecting argument that seven hospitals remaining after a merger could not coordinate because hospital services are "complex and heterogeneous").[19]

Equally important, the strong likelihood that Heinz and Gerber would engage in coordinated interaction, as established by the extraordinary concentration levels and high entry barriers, should not be easily overcome at this preliminary stage.

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[19] Furthermore, Heinz's plans to eliminate many Heinz varieties and some varieties of Beech-Nut baby food and to consolidate all jarred baby food production at its facilities in Pittsburgh (jarred) and Ontario (cereal) (DX 1 at 032; SApp. 5626) would in fact leave the market with less product differentiation.

This is an issue clearly appropriate for full adjudication in an administrative trial. The district court's unwillingness to allow for a more thorough inquiry into how this very concentrated market will function is inconsistent with the Congressional purpose of Section 13(b), to enjoin acquisitions so the Commission can conduct a trial on complex legal and economic issues. *See University Health,* 938 F.2d at 1225 (public interest "best served" by injunction pending full administrative review on the merits).

II. The District Court Erred In Uncritically Accepting Defendants' Efficiencies Defense.

As this Court recognized in granting the Commission emergency relief in this case, efficiencies "is a novel defense, which the Supreme Court has not addressed since the 1960s (and then, unfavorably) . . . , which this court has never addressed, and as to which the antitrust enforcement agencies have only recently clarified their views." Mem. Op. 2 (citations omitted); App. 1473. Despite the uncertain role of the efficiencies defense, the lower court found that the merger would result in savings of $9.4 to $12 million per year and would lead to innovation in the baby food market. In so holding, the district court, without any close examination, uncritically embraced and gave dispositive weight to all the efficiencies claimed by

Heinz at the preliminary injunction stage.[20] In so ruling, the court applied an incorrect legal standard to the treatment of efficiencies, and overlooked numerous flaws, both legal and factual, in defendants' efficiencies arguments.

A. Only An Extraordinary Showing of Efficiencies Could Possibly Justify A Merger In Such A Highly Concentrated Market.

Under the circumstances of this case – the attempted creation of a duopoly protected by high entry barriers – such uncritical acceptance of efficiencies claims is unwarranted. As this Court observed: "although there is much to be said for recognizing an efficiencies defense in principle, the high concentration levels present in this case complicate the determination of whether it should be permitted here." Mem. Op. 2; App. 1473. Indeed:

> Mergers in [the highly concentrated range] should carry a strong presumption of illegality that can be defeated only by a showing of extraordinarily easy entry or truly extraordinary efficiencies.

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[20] It is informative to contrast the district court's efficiencies analysis in this case (Op. 20-24; App. 1435-39) with the same court's efficiencies analysis in two other recent cases: *Cardinal Health*, 12 F. Supp.2d at 61-63; and *Staples*, 970 F. Supp. at 1088-90. Both cases question whether an efficiencies defense can overcome a *prima facie* case in a preliminary injunction. 12 F. Supp.2d at 61; 970 F. Supp. at 1088. The district court here wholeheartedly embraces the efficiencies defense at that stage. Both *Cardinal Health* and *Staples* hold that, even if an efficiencies defense can be entertained, defendants must show that the "proven" efficiencies will be passed on and that they overwhelm any possible anticompetitive effects of the merger. 12 F. Supp.2d at 63; 970 F. Supp. at 1090-91. Here the court below finds it sufficient that efficiencies merely exist.

Antitrust Law at ¶ 932, at 160; *id.* at ¶ 971f; *Merger Guidelines,* § 4.0 ("[e]fficiencies almost never justify a merger to monopoly or near-monopoly").

The reason why defendants must establish "extraordinary" efficiencies in highly concentrated markets with high entry barriers is straightforward.[21] Rivalry is the force that drives efficiency; without that rivalry there is no assurance that efficiency will be achieved or its benefits will result in a more competitive marketplace.[22] "[E]xperience teaches that without worthy rivals ready to exploit lapses in competitive intensity, incentives to develop better products, to keep prices at a minimum, and to provide efficient service over the long term are all diminished to the detriment of consumers." *PPG,* 628 F. Supp. at 885, *aff'd in relevant part*,

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[21] Some studies show that firms often fail to accomplish the projected cost savings from a merger. *See generally*, Conrath and Widnell, "Efficiency Claims in Merger Analysis: Hostility or Humility?," 7 George Mason L. Rev. 685 (1999); Brodley, "Proof of Efficiencies in Mergers and Joint Ventures," 64 Antitrust L.J. 576 (1996).

[22] Indeed, the district court voiced serious doubts about whether any of the claimed efficiencies will improve the competitive landscape or result in lower prices: "[w]hether Heinz will use the considerable cost savings from the merger to mount a vigorous campaign against Gerber for shelf space and market share remains to be seen." Op. 23; App. 1438. "Remains to be seen" is not the standard that courts or enforcement agencies have adopted to determine whether efficiencies are sufficient to overcome the anticompetitive aspects of the merger. *See University Health*, 938 F.2d at 1223.

798 F.2d 1500 (D.C. Cir. 1986).[23] And as the *Merger Guidelines,* § 4.0, explain, "[w]hen the potential adverse competitive effect of a merger is likely to be particularly large, extraordinarily great cognizable efficiencies would be necessary to prevent the merger from being anticompetitive."[24] Here, because the efficiencies are not extraordinary, the district court should have preserved the Commission's chance to fully evaluate defendants' efficiencies claims in a proceeding on the merits.

B. Defendants' Proffered Efficiencies Are Speculative And Not Legally Cognizable.

Even assuming, *arguendo*, that – in cases challenging mergers to monopoly or near monopoly – a preliminary injunction proceeding is an appropriate stage at which a court might entertain a full efficiencies defense, it is plain that the district court erred in crediting the defense here.[25] First, the efficiencies are speculative and

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[23] *See also United States v. Western Elec. Co.*, 592 F. Supp. 846, 874 (D.D.C. 1984), *appeal dismissed*, 777 F.2d 23 (D.C. Cir. 1985) (competition results in "lower prices, highest quality, and the greatest material progress").

[24] The only appellate court to address efficiencies has held that defendants "must demonstrate . . . [the merger's] economies ultimately would benefit competition and, hence, consumers." *University Health*, 938 F.2d at 1223.

[25] Other courts have been very cautious in recognizing efficiency claims – even in markets that are far less concentrated than this one – because these claims are far easier to assert than to achieve. *See* n.21, *supra.* For that reason, the courts have imposed a "very rigorous" evidentiary burden on parties seeking to justify a

are by no means "proven" on this preliminary injunction record, and in any event are so modest that they would easily be swamped by an anticompetitive price increase. Second, even if defendants' efficiencies had been "proven," they are not cognizable because (a) they depend on a reduction in output (a loss of consumer choice); (b) they are achievable by other means; and (c) they depend on the notion – entirely inapplicable here – that mergers should be allowed when they enable two small competitors to compete better against a larger firm.

1. The Claimed Efficiencies Are Speculative and Would Be Swamped By Any Anticompetitive Price Increase.

The court below concluded that the proposed merger would produce benefits that would be "immediate and virtually automatic," assuming that the merged firm

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merger with an efficiencies defense, by requiring them to demonstrate that claimed efficiencies: (1) are identified with precision, *i.e.,* are not based on "speculation," can be verified and actually will be achieved, (2) are "cognizable," *i.e.*, they do not result from an anticompetitive reduction in output or quality; (3) are "merger-specific," *i.e.*, they cannot be achieved by other means less restrictive of competition, (4) will be passed on, and produce a significant economic benefit to customers; and (5) will outweigh the anticompetitive effects of the acquisition and result in a more competitive market. *See University Health*, 938 F.2d at 1222-23; *Cardinal Health*, 12 F. Supp.2d at 61-63; *Staples,* 970 F. Supp. at 1089-91; *United States v. United Tote*, 768 F. Supp. 1064, 1084-85 (D. Del. 1991) (efficiencies rejected because "there are no guarantees that these savings will be passed on to the consuming public"); *United States v. Rockford Mem. Corp.*, 717 F. Supp. 1251, 1289 (N.D. Ill. 1989), *aff'd*, 898 F.2d 1278 (7th Cir. 1990); *Ivaco*, 704 F. Supp. at 1425-27.

would instantly improve the quality of Heinz's products and reduce the prices paid by Beech-Nut customers. Op. 23; App. 1438. That conclusion, so central to the lower court's refusal to grant a preliminary injunction, rests on numerous legal and factual errors.

Although the court claimed not to be "accepting at face value the aspirational testimony of Heinz executives," it offered no other basis for its pivotal assumption that the merged firm would pursue a policy of "value pricing," rather than maintaining current Beech-Nut prices and pocketing any cost savings. *See id.* Moreover, as we have demonstrated above, the creation of a durable duopoly affords both the opportunity and incentive for all firms to increase prices. This proposition, overlooked by the district court, is critical, for even a modest increase in prices would swamp the efficiencies defendants assert. Even if the court below were correct in accepting the claimed cost savings of $9.4 to $12 million, those figures are incredibly modest in relation to sales in the market, which the court found to be "$865 million to $1 billion." *Id.* at 2; App. 1417. Since even a minimal anticompetitive price increase of 2% (about a penny per jar) would overwhelm the claimed efficiencies, the court's full crediting of such modest efficiencies is

stunning, especially in a market where Gerber regularly increases prices, and Heinz follows. *Id*. at 4; App. 1419.[26]

Furthermore, contrary to the district court's assumption, the record below shows that the claimed cost efficiencies are far from proven. For example, one of defendants' most critical assumptions is that the combined company will retain 100% of the customers of the separate companies after the merger.[27] PX 762 at 145; App. 3895. Nothing in the record supports that assumption. Loyal users of each brand strongly prefer that brand over others. PX 98 at 627; App. 1967. Indeed, ****************** highlights the importance ********************* *** ************************* PX 533 at 70; PX 694 at 55-57 *************** ***

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[26] The prospect that efficiencies would be overcome by the anticompetitive aspects of a merger-to-duopoly has, quite properly, led other courts uniformly to reject efficiency claims in such cases. *See United Tote,* 768 F. Supp. at 1071-72; *Ivaco*, 704 F. Supp. at 1428 & n.18.

[27] The estimates are also based on another critical assumption: that Heinz will have no problem in reducing the number of combined company SKUs from the current total of 258 (128 Beech-Nut + 130 Heinz) to approximately 130 after the merger. PX 696 at 113; App. 3700. Heinz performed no analyses to assess the impact on cost savings of any slippage from any of its critical assumptions. Tr. 732; App. 816.

**************** App. 3064, 3550-51; *see also* PX 149; App. 2080-81. Any post-merger reduction in the sales, of course, would translate directly into a reduction in the cost savings that defendants claim (and the court accepted). Tr. 781-82; App. 865-66. In light of this and numerous other serious flaws in defendants' showing of supposed efficiencies, it was error for the district court precipitously to accept such claims at the preliminary injunction stage, rather than preserving the Commission's ability to examine these speculative claims in a full evidentiary hearing.[28]

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[28] Numerous errors merit further study; for example, the efficiencies estimates presented to the court: (1) are substantially lower than the "cautious" estimates Heinz has developed for internal use (PX 696 at 191-92; App. 3719; *see id*. at 63-67; Tr. 711-13, 772-78; PX 581 at 252; DX 122, 124; App. 3687-88, 795-97, 856-62, 3109, 4616, 4618); (2) are based on outdated cost information for Beech-Nut (PX 612 at 637; Tr. 729-730; App. 3167, 813-14), which lead to overstated cost savings (*see* PX 762 at 52-53, 113-14; Tr. 791-92; PX 612 at 637; App. 3871-72, 3887, 875-76, 3167); (3) are in part based upon projections made for defendants by Booz, Allen & Hamilton (PX 696 at 54-56; App. 3685) that defendants failed either to verify or to support in the preliminary injunction proceeding (PX 696 at 169-75; PX 762 at 42-44; Tr. 770; App. 3714-15, 3869, 854); (4) fail to consider fully the impact, if any, that the increases in production at Heinz's facility would have upon Heinz's cost structure (*see* Tr. 721-25; PX 696 at 155-156; App. 805-09, 3710); (5) are not computed against a (higher) cost baseline that includes any new products that Heinz might allegedly produce after the merger (Tr. 733-34; PX 696 at 140; App. 817-18, 3706); and (6) fail to account for the likely loss of sales of jarred baby food, assuming Heinz actually introduces the products that it says it has under development (Tr. 733, 782-84; PX 762 at 139-40; App. 817, 866-68, 3893).

The district court also erred in accepting at face value Heinz's rosy predictions of innovations the merger would supposedly allow it to introduce to American consumers. In fact, the two new "products" the defendants identified either do not exist or may not be commercially feasible. They are therefore entirely speculative. For example, ** ** *************************************** PX 694 at 237-38; App. 3596; *see* PX 761 at 79; App. 3856. Similarly, Heinz has not even decided whether to fund any aseptic products for the domestic market (Tr. 636-38, 641, 643-46; App. 718-20, 723, 725-28) and the company has genuine concerns about whether aseptic products can gain consumer acceptance.[29] Tr. 639-41, 646-47; PX 694 at 76-77, 84-86; App. 721-23, 728-29, 3555-58. The record shows that **************************** *** PX 440 at 576 (Heinz needed a "tangible growth plan" or the deal would be "DOA in Washington"); PX 487 at 105; Tr. 644-45; App. 2718, 2925, 726-27. Under the

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[29] Heinz's CEO characterizes the work thus far as "preliminary research" (Tr. 527; App. 611); PX 689 at 143 ("aseptic right now is an unproven and eventually – it's a small proposition right now"); PX 682 at 06; App. 3399, 3213; *see also* PX 437; App. 2716.

best conditions, even assuming aseptic baby food is technically feasible (*see* Tr. 640-641; App. 722-23), ** *** PX 695 at 134; PX 440 at 575-76; PX 647; App. 3650, 2717-18, 3189; *see also* PX 664; App. 3190-94.

A merger in a highly concentrated market should not be approved on the basis of "speculative and self-serving assertions" proffered in a preliminary injunction hearing. *University Health*, 938 F.2d at 1223; *see Ivaco*, 704 F. Supp at 1426 (rejecting claims based on aspirational testimony).

2. The Claimed Efficiencies Are Not Cognizable.

(a) The Efficiencies Depend On A Reduction In Output.

Defendants' vaunted efficiencies are not cognizable because they result from an anticompetitive reduction in consumer choice. Defendants plan to discard about 120-130 SKUs as a result of the merger – nearly 1/2 of their combined product line. PX 696 at 113; Tr. 730-31; App. 3700, 814-15; *see* n.27, *supra*. The merger will thus result in a significant reduction in choice and quality. PX 782 at ¶¶ 99-102; App. 4047-49.[30] Although moving production to Heinz's plant may lower

[30] This fact itself refutes the district court's supposition that the merger would yield "immediate and virtually automatic" benefits to consumers with respect to product quality. *Cf.* Op. 23; App. 1438. Moreover, the benefits of competition

production costs, consumers who prefer the discarded recipes or Beech-Nut's (or Heinz's) quality may be worse off. *See* PX 482 at 88 (customers were upset when Albertson's switched to Heinz); App. 2893. Indeed, consumer choice is an important factor in baby food, including choice in price and quality.[31] Tr. 297; App. 332; *see* PX 98 at 618; App. 1966.

(b) The Efficiencies Can Be Achieved Without The Merger.

A major component of Heinz's efficiencies defense is its claim that the merger will give it sufficient market penetration to allow it to introduce new products. However, **
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****************** PX 695 at 44; App. 3630.

Since the new products require entirely new equipment and facilities, their production does not depend upon Heinz's acquiring Beech-Nut. Indeed, Heinz

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which Section 7 is designed to preserve include "unquantifiable efficiencies in 'all elements of a bargain – quantity, service, safety, and durability – and not just the immediate cost.'" *FTC v. Alliant Techsystems, Inc.,* 808 F. Supp. 9, 23 n.5 (D.D.C. 1992), *quoting National Soc'y of Prof. Eng'rs v. United States*, 435 U.S. 679, 695 (1978).

[31] *See also* Pitofsky, "Efficiencies in Defense of Mergers," 7 Geo. Mason L. Rev. 485, 486-87 (1999) ("efficiencies must not arise from anticompetitive reductions in output, service, or other competitively significant categories such as innovation").

recognizes that even with the merger, it may be better to enter a copacking arrangement than to purchase equipment initially. PX 695 at 67; App. 3636. Since aseptic does not involve jarred production equipment, the aseptic "innovation" could be accomplished without the merger. PX 821; Tr. 301-02; App. 4276-77, 337-38.

The district court implicitly found, however, that Heinz cannot market aseptic products because it has inadequate market penetration, which it can only remedy by joining forces with Beech-Nut. *See* Op. 23-24; App. 1438-39. But this ignores the fact that the antitrust laws do not prohibit competitors from forming joint ventures or other limited arrangements to develop, produce, and even market new products. *See* Antitrust Guidelines for Collaborations Among Competitors (April 2000). Heinz is free to perfect and market aseptic baby food, by entering into an appropriately structured joint venture or other arrangement with Beech-Nut (or other firms) to develop that product. *See PPG,* 798 F.2d at 1508 ("cooperation with other market participants could yield similar results without causing the same market concentration").

(c) The Merger Is Not An Appropriate Means Of Improving Competition With Gerber.

The district court credited the defendants' claim that the merger was the only way to challenge Gerber's dominance (Op. 23-24; App. 1438-39) – a strained

variation of the "small competitor" defense articulated in *Brown Shoe Co. v. United States*, 370 U.S. 294 (1962). That defense would allow a merger that enables "two small companies . . . to enter into more meaningful competition with those [companies which are] dominating the relevant markets." 370 U.S. at 346.[32] Significantly, this argument failed in *Brown Shoe,* where the merging firms had far smaller market shares, and has rarely been accepted.[33] The district court's acceptance of this defense was legal error. To begin with, this "defense" is totally misplaced in this market. Heinz and Beech-Nut are large profitable firms and would, if combined, possess over 34% of the jarred baby food market. The merging

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[32] Although the Clayton Act does not generally impede the merger of genuinely *small* companies, we are not aware of any case that has allowed a merger to go forward solely on the ground that the merged entity will be able to compete better against a dominant firm. *See* American Bar Association, Mergers and Acquisitions 137 (2000) ("arguments that increased market share will improve competition in the market are . . . rarely successful or publicly endorsed by courts or the enforcement agencies"). *Brown Shoe* addressed the need of small firms to merge to compete more effectively "with larger *corporations* dominating the relevant market." 370 U.S. at 319; *see United States v. Philadelphia Nat'l Bank*, 374 U.S. 321, 370-71 (1963). Nothing in the legislative history of Section 7 suggests that firms might merge in order to create a duopoly.

[33] *See Ford Motor Co. v. United States*, 405 U.S. 562, 569-70 (1972) (rejecting argument that acquisition would have beneficial effect because it would make third firm in market "a more vigorous and effective competitor against" the top two firms); *RSR Corp. v. FTC*, 602 F.2d 1317, 1325 (9th Cir. 1979) (declining to approve merger which increased the merged firm's market share from 12% to 19%, because "a merger of the second and fifth largest firms . . . is not the merger of 'two small firms.'"); *United Tote,* 768 F. Supp. at 1084; *FTC v. Lancaster Colony Corp.*, 434 F. Supp. 1088, 1095 (S.D.N.Y. 1977); *United States v. Bethlehem Steel Corp.*, 168 F. Supp. 576, 618 (S.D.N.Y. 1958).

parties in this case do not remotely qualify for any "small company" defense, assuming *arguendo* that one exists.

More important, the lower court should not even have considered defendants' assertions that the merger was needed to enable the combined company to compete better with Gerber. The court's logic turns Section 7 on its head, by permitting mergers *because* markets *are* concentrated. Where firms compete against more dominant rivals, this argument would permit even more consolidation of power. It would permit every market in which there is a dominant firm to merge into a duopoly. This is directly contrary to the Supreme Court's teaching in *United States v. General Dynamics Corp.*, that "if concentration is already great, the importance of preventing even slight increases in concentration is correspondingly great." 415 U.S. 486, 497 (1974), *quoting Aluminum Co. of America*, 377 U.S. at 279. A concentrated market does not become more competitive by permitting significant competitors to consolidate. Indeed, such an approach is inconsistent with the law and sound antitrust policy, which prefers "growth by internal expansion . . . to growth by acquisition." *Philadelphia Nat'l Bank*, 374 U.S. at 370.

Given the high entry barriers into the baby food market and the merger's effect on concentration in this already highly concentrated market, the district court erred in giving conclusive weight to defendants' inadequately established efficiencies and innovation claims. As this Court observed in *Baker Hughes,*

"[p]redicting future competitive conditions in a given market . . . calls for a comprehensive inquiry." 908 F.2d at 988. This, of course, is precisely the point here. The district court should have granted the Commission a preliminary injunction so it could undertake the "comprehensive inquiry" that this case requires. This position fully comports with this Court's observation in this case that "appellees' efficiencies defense may yet carry the day" (Mem. Op. 3; App. 1474), but if that is to happen, it should be later in the day, after defendants' claims have been carefully examined in the full light of a trial on the merits.

III. The Lower Court Erred In Weighing The Equities.

Section 13(b) of the FTC Act provides that the Commission is entitled to a preliminary injunction if a court determines that one is in the "public interest" after "weighing the equities and considering the Commission's likelihood of success." 15 U.S.C. § 53(b). Here, the lower court gravely misapplied that standard, by concluding that the equities favored the defendants because a preliminary injunction *might* result in their terminating the merger (Op. 27; App. 1442) even though the court also concluded that:

> [I]f the merger is allowed to proceed before the full-scale administrative proceedings contemplated by the Federal Trade Commission Act can be had, the outcome of such proceedings will not matter, because [Beech-Nut's] Canajoharie plant will be closed, the Beech-Nut distribution channels will be closed, the new label and recipes will be in place, and it will be impossible as a practical matter to undo the transaction.

Id. at 26-27; App. 1441-42. This was serious error and defendants' threat to abandon the transaction should have been accorded no weight at all.

Indeed, nothing in the record supports the claim that an injunction would "kill the merger." On the contrary, the record shows that Beech-Nut is not about to look for alternative buyers, and Heinz's officials are eager to consummate the transaction. Nor will the efficiencies the parties assert disappear if consummation is delayed while the merger is considered fully. As this Court observed here: "even if current merger plans were abandoned, the evidence does not establish that the efficiencies the appellees urge could not be reclaimed by a renewed transaction." Mem. Op. 2; App. 1473. The district court's concern that the parties might "kill the merger" is based wholly on unsupported argument.

The premerger notification statute and regulations have been part of the merger landscape for many years. Sophisticated business enterprises (like defendants) who retain experienced and highly skilled counsel, as defendants have here, know how long the antitrust review process takes, and they can reasonably expect that a merger to duopoly would not go unnoticed by the antitrust enforcement

agencies.[34] There is no basis for the district court to entertain the suggestion that a preliminary injunction should be denied because any delay might cause the defendants to abandon their merger plans.

Perhaps realizing the weakness of defendants' argument, the lower court attempted to skate lightly over this thin ice by asserting that this factor merely "tips" the balance in defendants' favor. Op. 28; App. 1443. However, defendants' threat to abandon the transaction is the *only* "equity" that the court cited in juxtaposition to the harm to the public interest that would result from the merger's being consummated before the Commission's challenge could be heard on the merits. That was not a sufficient (or even cognizable) reason – the disappointment of private expectations that inevitably results when an acquisition is enjoined is simply no reason to deny injunctive relief. *PPG*, 798 F.2d at 1506-08. Indeed, the Ninth Circuit, in *Warner Communications,* under similar circumstances granted an

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[34] *See* PX 313 at 011, 013 ***
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*********************** App. 2508, 2510.

injunction but ordered the Commission to expedite its administrative proceeding.[35]

742 F.2d at 1165. Similarly, the Eleventh Circuit observed in *University Health*:

> [T]he FTC only asks for a preliminary injunction; if the appellees can demonstrate the legality of the proposed acquisition to the FTC or, ultimately, the court of appeals, the acquisition will take place. We do not think that this delay, in and of itself, will spell disaster for [the acquired firm] or grave harm to the public. *Rather, we think the public will be best served by enjoinment of this acquisition pending extensive analysis of its competitive effect.*

938 F.2d at 1225 (emphasis added). The district court here committed legal error in according defendants' self-serving private equity claim conclusive weight against serious public concerns. *Id.; Warner Communications,* 742 F.2d at 1165.

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[35] The district court in *Staples,* 970 F. Supp. at 1093, likewise recognized that an injunction "will most likely kill the merger" and affect shareholders, but deemed that private equity insufficient to overcome the public interest in enjoining the transaction.

CONCLUSION

For the foregoing reasons, the decision of the district court should be reversed and the matter remanded to that court with instructions to enter a preliminary injunction.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE PURSUANT TO FED. R. APP. P. 32(A)(7)(c) AS TO WORD COUNT

I certify that pursuant to Fed. R. App. P. 32(a)(7)(C) the Brief of Appellant Federal Trade Commission is proportionally spaced, has a typeface of 14 points, and contains 13,830 words.

____

David C. Shonka

STATUTES AND REGULATIONS

Section 13(b) of the FTC Act, 15 U.S.C. § 53(b), provides in pertinent part:

> (b) Whenever the Commission has reason to believe--
>
> (1) that any person, partnership, or corporation is violating, or is about to violate, any provision of law enforced by the Federal Trade Commission, and
>
> (2) that the enjoining thereof pending the issuance of a complaint by the Commission and until such complaint is dismissed by the Commission or set aside by the court on review, or until the order of the Commission made thereon has become final, would be in the interest of the public--
>
> the Commission by any of its attorneys designated by it for such purpose may bring suit in a district court of the United States to enjoin any such act or practice. Upon a proper showing that, weighing the equities and considering the Commission's likelihood of ultimate success, such action would be in the public interest, and after notice to the defendant, a temporary restraining order or a preliminary injunction may be granted without bond . . . .

Section 7 of the Clayton Act, 15 U.S.C. § 18, provides in pertinent part:

> No person engaged in commerce or in any activity affecting commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital and no person subject to the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets of another person engaged also in commerce or in any activity affecting commerce, where in any line of commerce or in any activity affecting commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly.

CERTIFICATE OF SERVICE

I hereby certify that I have this 29nd day of November, 2000, served the Joint Appendix, the Supplement to the Appendix, and two copies of the Federal Trade Commission's Brief by hand delivering copies to:

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