UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF KENTUCKY
LONDON DIVISION

	)	
UNITED STATES OF AMERICA, et al.,	)	**REDACTED VERSION**
	)	Confidential Information
Plaintiffs,	)	Redacted
	)	
v.	)	Civil Action No.: 6:03-206-KSF
	)	
DAIRY FARMERS OF AMERICA, INC., et al.,	)	
	)	
Defendants.	)	
	)	

PLAINTIFFS' MEMORANDUM IN SUPPORT OF ITS MOTION FOR PARTIAL SUMMARY JUDGMENT ON DFA'S "CONTROL" AFFIRMATIVE DEFENSE

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PLAINTIFFS' MEMORANDUM IN SUPPORT OF ITS MOTION FOR PARTIAL SUMMARY JUDGMENT ON DFA'S "CONTROL" AFFIRMATIVE DEFENSE

Introduction

Through the transaction challenged in this case, Dairy Farmers of America, Inc. (DFA) acquired a 50% common ownership interest and a 100% preferred interest in two dairies, Southern Belle Dairy Co., LLC and National Dairy Holdings, LP (NDH)—the only two competitors for school milk in 46 school districts in Kentucky and Tennessee. For an additional 50 school districts in those states, the two dairies are two of the only three competitors for school milk. Many of these school districts were victims of a confessed bid-rigging cartel that Southern Belle and Flav-O-Rich, an NDH dairy located roughly thirty miles from Southern Belle, ran from the late 1970s to 1989, vividly demonstrating the dairies' ability to raise prices.

DFA's principal defense of its acquisition is that DFA "cannot control" either of the dairies, despite holding a 50% common interest and all of the preferred interests in the two. *See Answer of Defendant Dairy Farmers of America, Inc. to Amended Complaint* at 10 (DFA's second affirmative defense). This defense fails as a matter of law, and the United States and the Commonwealth of Kentucky are entitled to partial summary judgment under Fed. R. Civ. P. 56. According to DFA's theory, consolidating all the competitors in a market under the ownership structure that DFA designed here prevents even a *reasonable probability* that the consolidated companies will avoid vigorous competition to undercut each other's prices. DFA must also argue that this is true even though the companies involved have a demonstrated history of colluding and successfully raising prices above competitive levels. The untenable breadth of DFA's argument is quickly illustrated: If DFA were correct, the defense would permit the total consolidation of any industry under a single holding company, so long as the parent holds "only" a 50% common equity interest in all the acquired companies (while still holding all the preferred equity). The argument proves too much.

DFA will undoubtedly complain that it may contest the market facts that the government intends to prove. But the defense, by DFA's own logic, is supposed to defeat the government's case as alleged. Accordingly, partial summary judgment on this defense will streamline the issues, leaving the market facts for resolution at trial.

Overview of the Argument

To assist the Court in ruling on DFA's principal defense now (and to avoid days of trial over these "control" or "governance" issues), this brief addresses seven key points:

- Acquisitions, including partial acquisitions, are illegal under Section 7 of the Clayton Act, 15 U.S.C. § 18, when they pose a *reasonable probability* of anticompetitive cooperation or collusion among companies in the relevant market. Moreover, courts presume that further consolidation in an already highly concentrated market is illegal.

- Any valid defense to this transaction must overcome the *strong presumption against combining two companies previously convicted of bid rigging*. The market-allocation scheme used by Flav-O-Rich and Southern Belle was also easy to carry out, increasing the probability of anticompetitive harm.

- Section 7 of the Clayton Act, by its express terms, applies to partial acquisitions, and the Supreme Court has made clear that *"control" is not required* under the law. Moreover, no court has ever ruled that an otherwise illegal transaction was exonerated because the parent held "only" 50% of the common equity and all of the preferred interests.

- DFA's defense fails under Section 7 because the acquisition *gives DFA an incentive and opportunity* that it did not previously have to lessen competition between Southern Belle and NDH. The defense also fails because *Southern Belle now has an added incentive not to compete* against another DFA dairy, Flav-O-Rich. Given that the transaction gives all three companies, Southern Belle, NDH, and DFA, an incentive and opportunity to reduce competition, DFA's "control" defense fails to negate a reasonable probability of anticompetitive harm.

- Cooperation between the dairies is made even more likely by the uncontroverted history of friendly financial dealings between DFA and the executives whom DFA selected to head both Southern Belle and NDH. This history of close and mutually beneficial dealings underscores that *DFA's hand-picked partners are highly unlikely to compete against each other*, causing financial losses to themselves and DFA.

- Even well-recognized antitrust defenses, like efficiencies and entry, are seldom accepted in markets as concentrated as these, where the transaction reduces the number of competitors from two to one or three to two—*the most concentrated markets possible in antitrust analysis*.

- The caselaw, including longstanding law from the Sixth Circuit, firmly establishes the *irrelevance of all of defendants' anticipated testimony* that DFA does not intend to raise school milk prices and that it promises that its family of affiliates will engage in cutthroat competition with each other.

Argument

I. An acquisition violates Section 7 when it poses a reasonable probability of increasing cooperation or coordination among competitors in the market.

Section 7 of the Clayton Act employs an incipiency standard—arresting competitive problems before they occur. Thus, plaintiffs "need only prove that [the transaction's] effect '*may be* substantially to lessen competition'" within the relevant market. *California v. American Stores Co.*, 495 U.S. 271, 284 (1990) (quoting 15 U.S.C. § 18) (emphasis in original). By proscribing transactions that "may" substantially lessen competition, Congress "indicate[d] that its concern was with probabilities, not certainties." *FTC v. H.J. Heinz Co.*, 246 F.3d 708, 713 (D.C. Cir. 2001) (quoting *Brown Shoe Co. v. United States*, 370 U.S. 294, 323 (1962)).

Section 7 does not require proof that higher, anticompetitive prices have occurred in the affected market. *Hospital Corp. of America v. FTC*, 807 F.2d 1381, 1389 (7th Cir. 1986) (Posner, J.). "All that is necessary is that the merger create an appreciable danger of such consequences in the future. A predictive judgment, necessarily probabilistic and judgmental rather than demonstrable is called for." *Heinz*, 246 F.3d at 719 (quoting *Hospital Corp. of America*, 807 F.2d at 1389). *See also United States v. Philadelphia Nat'l Bank*, 374 U.S. 321, 362 (1963). Although speculation is insufficient, the government satisfies its burden by showing a "reasonable probability," *United States v. E.I. du Pont de Nemours & Co.*, 353 U.S. 586, 589 (1957), and need not establish a "high probability" of anticompetitive harm. *FTC v. Elders Grain*, 868 F.2d 901, 906 (7th Cir. 1989) (Posner, J.). And "doubts are to be resolved against the transaction." *Id.* (citing *Philadelphia Nat'l Bank*, 374 U.S. at 362-63; *United States v. Falstaff Brewing Corp.*, 410 U.S. 526, 555-58 (1973)).

In making a predictive judgment about whether a transaction poses a reasonable probability of anticompetitive effects, courts typically determine (1) the affected "line of commerce," or product market, (2) the affected "section of the country," or geographic market, and (3) whether the transaction may substantially lessen competition in the defined product and geographic market, often together referred to as the "relevant market." *See, e.g., United States v. Marine Bancorp.*, 418 U.S. 602, 618-23 (1974).

By defining a relevant product and geographic market in steps (1) and (2) above, a court can evaluate how concentrated the market is. Transactions that increase concentration in an already highly concentrated market are presumed to cause the anticompetitive effects in step (3) above. As the Supreme Court has said, a merger that "produces a firm controlling an undue percentage share of the relevant market, and results in a significant increase in the concentration of firms in that market, is so inherently likely to lessen competition substantially that it must be enjoined in the absence of evidence clearly showing that the merger is not likely to have such anticompetitive effects." *United States v. General Dynamics Corp.*, 415 U.S. 486, 497 (1974) (quoting *Philadelphia Nat'l Bank*, 374 U.S. at 363). *See also Hospital Corp. of America*, 807 F.2d at 1388.

A principal reason that increasing market concentration can reduce competition is that it facilitates cooperation or collusion between firms in the market. Thus, it is often said that the presumption of illegality "rests upon the theory that, where 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." *H.J. Heinz Co.*, 246 F.3d at 715 (quoting *FTC v. PPG Indus.*, 798 F.2d 1500, 1503 (D.C. Cir. 1986) (Bork, J.)). *See also Elders Grain*, 868 F.2d at 905.

Measures of market share and concentration, "while of great significance," are not, of course, "conclusive indicators of anticompetitive effects." *Heinz*, 246 F.3d at 717 n.12 (citing *General Dynamics Corp.*, 415 U.S. at 498; *Brown Shoe*, 370 U.S. at 322 n.38). Once the government establishes the presumption of illegality based on the market concentration, the defendants "must produce evidence that 'shows that the market-share statistics give an inaccurate account of the merger's probable effects on competition' in the relevant market." *Heinz*, 246 F.3d at 715 (quoting *United States v. Citizens & S. Nat'l Bank*, 422 U.S. 86, 120 (1975) (brackets omitted)).

DFA's so-called "control" defense is presumably intended as rebuttal evidence showing its purported lack of influence eliminates a reasonable probability of anticompetitive harm. The defense fails to do that, and therefore this Court should grant summary judgment, striking the defense.

II. A valid defense must overcome the presumption against joining parties to a bid-rigging scheme.

For DFA's defense to be valid, it must not only overcome the presumption created by the market concentration, but also a presumption against combining companies with a history of bid rigging. Even where there is evidence of past cooperation by firms that *falls short* of price fixing or bid rigging, courts have been reluctant to approve mergers in that market. "[A] market in which competitors are unusually disposed to cooperate is a market prone to collusion. The history of successful cooperation establishes a precondition to effective collusion—mutual trust and forbearance, without which an informal collusive arrangement is unlikely to overcome the temptation to steal a march on a fellow colluder by undercutting him slightly." *Hospital Corp. of America*, 807 F.2d at 1388.

But in this case there is much more than just past cooperation between the two dairies: Flav-O-Rich and Southern Belle engaged in outright bid rigging of milk to school districts in Kentucky for a decade. Statement of Facts (SF) at ¶ 30. This evidence greatly strengthens the case for finding the transaction illegal and therefore increases the demands placed on any defense. As a leading antitrust treatise, cited more than forty times by the Supreme Court, has said, "where the evidence establishes previous *attempts* to engage in price fixing, any significant merger by one of the firms involved in the attempts should be presumptively unlawful." 4 Phillip E. Areeda, John L. Solow, & Herbert Hovenkamp, *Antitrust Law* ¶ 917 at 90 (rev. ed. 1998) (emphasis added). And of course what transpired in this case were not mere feints and attempts at collusion, but a complete and durable scheme. Indeed, plaintiffs are not aware of any litigated case in the history of the antitrust laws where a court ruled in favor of a merger between the only two participants of a long and successful bid-rigging scheme.

The presumption against joining former bid riggers is distinct from the presumption based on market concentration. Areeda and Hovenkamp conclude that when a history of collusion exists, a merger may be blocked even where "structural evidence alone would be insufficient." *Id.* In other words, even if the usual standards for defining a market and measuring its concentration failed to give rise to a presumption of illegality, a history of collusion could itself suffice to establish the illegality of the merger.

Taken together, the two presumptions, based on separate but reinforcing methods of gauging likely anticompetitive effects, heighten the hurdle that any defense to this transaction must clear. *Cf. FTC v. Indiana Federation of Dentists*, 476 U.S. 447, 460-61 (1986) ("proof of actual detrimental effects, such as a reduction of output, can obviate the need for an inquiry into market power, which is but a surrogate for detrimental effects.") (quotation marks omitted). *See also Elders Grain*, 868 F.2d at 905 (noting in a merger case the value of "a history of efforts to fix prices in the industry—a history that predates the market structure even more prone to collusion that the challenged acquisition created"). Combining former bid riggers raises a real threat to competition and therefore requires a compelling defense.

The history of bid rigging is also significant because the mechanism that the dairies used to accomplish the bid rigging was so simple, demonstrating how little would be required to diminish competition now that DFA has installed its hand-picked partners at the head of Southern Belle and Flav-O-Rich. To accomplish the bid rigging, Southern Belle and Flav-O-Rich assigned different customers to the two dairies. SF ¶ 30-36. Because bids for school milk were submitted only once per year, the process was simple: Each dairy just submitted a high bid where the other dairy had an existing account. *Id.*. Contrary to defendants' repeated assertions, this scheme, like many market-allocation schemes, did not require the dairies to exchange district-by-district pricing information. *See, e.g., Palmer v. BRG of Georgia, Inc.*, 498 U.S. 46, 48-49 (1990) (*per curiam*) (market allocation accomplished without an exchange of pricing information). As Maurice Binder, a Flav-O-Rich employee involved in the bid rigging, explained, "The procedure was that I was to keep what accounts that I had, and [the Southern Belle employee] was to keep what he had. And we would protect each other in the bidding process." SF ¶ 33.

This procedure is a natural one in the industry.

SF ¶ 37. The same logic of course applies to DFA and its affiliates.

SF ¶ 38.

In 1997, Southern Belle described an incident that provides a striking illustration of how easy it would be to restart the market allocation, or simply lessen the vigor of the competition between the two dairies—an effect that would also be sufficient to render the acquisition illegal.

As Southern Belle's recounting of the incident highlights, the communication involved could not have been simpler:

> While attending the Casey County Kentucky Board of Education's scheduled meeting, held on June 2, 1997, for the purpose of opening submitted bids for milk and related products for the school year 1997-1998, Southern Belle Dairy Branch Manager, Justin Prewitt was approached by Flav-O-Rich employee Danny Moore, and the enclosed verbal exchange took place:
>
> Danny Moore: "How's your route volume holding out?"
>
> Justin Prewitt: "OK, but it could always be better."
>
> Danny Moore: "Have you bid a lot of schools already?"
>
> Justin Prewitt: "This is my first one."
>
> Danny Moore: "I'll just tell you. We're only bidding to get the schools that we had last year."
>
> At that point, Justin Prewitt made no reply, and walked away to avoid further conversation.

SF ¶ 39.

As this description illustrates, not much communication is necessary to lessen competition in markets with annual bids and few competitors.

III. Section 7 by its express terms applies to partial acquistions, and no showing of "control" is required.

By its express terms, Section 7 of the Clayton Act applies to partial acquisitions. The statute provides, "No person engaged in commerce . . . shall acquire, directly or indirectly, the whole *or any part* of the stock or other share capital" of another company where doing so may substantially lessen competition. 15 U.S.C. § 18 (emphasis added).

In evaluating a partial acquisition, and DFA's "control" defense in particular, it is important to emphasize that under the Clayton Act, "control" is not required: "A company need not acquire control of another company in order to violate the Clayton Act." *Denver & Rio Grande West R.R. v. United States*, 387 U.S. 485, 502 (1967). What matters is whether there is a reasonable probability that competition will be lessened. If there is such a risk, any absence of control is irrelevant. *Id.*

In keeping with its "control" defense, DFA has argued that it does not attempt to run the day-to-day operations of its dairy affiliates and takes a hands-off approach. But even if DFA were correct that control is necessary,

statements by credit agencies like Moody's reporting that "NDH is owned and controlled by its management and by DFA" and that "DFA's significant ownership and influence upon NDH [i]s a credit positive." SF ¶ 40-44.

SF ¶ 63.

In any event, whether or not DFA currently gets involved in the day-to-day operations of its dairies is legally irrelevant and insufficient to disprove the likelihood of anticompetitive effects.

The same logic applies to Southern Belle and NDH.

There is no reason to expect that either company will act against what is in the collective interest of all three. Southern Belle and NDH are both more profitable when they can charge higher prices, and DFA makes more money when its joint ventures are more profitable. But if for some reason one dairy did act against the collective interest of all three, DFA would have an incentive to correct the situation. And correcting the situation should be easy, given that reducing competition benefits all of them.

Areeda and Hovenkamp reach similar conclusions about the effects of partial acquisitions—and they do so without assuming a market as concentrated as this one, with a long and vivid history of collusion, and where, as described more fully below, the top executives can trust each other based on a track-record of mutually beneficial deals. A partial acquisition can dampen competition because it "effects some sharing of profits, reduces incentives for 'cheating' [by undercutting the higher prices], makes departures from agreed behavior harder to conceal, and thus seals the bargain of express collaboration." 5 *Antitrust Law* ¶ 1203c at 282 (2d ed. 2003). Areeda and Hovenkamp also note: "At the psychological level, either company might lose some of its former zeal to compete with the other. And, quite apart from any such feelings, the acquired firm may have good reason to direct its competitive energies away from the acquiring firm." *Id.* In light of these factors, "there is good reason for presumptively treating partial acquisitions, at least substantial ones, in the same way as full acquisitions." *Id.* at 283. And a deal involving 50% of the common interests and more than 95% of the preferred interests obviously constitutes a "substantial" partial acquisition. In short, when a company acquires interests so substantial, the fact that the equity interests are not 100% does not qualify as a defense to an otherwise illegal transaction.

This analysis is consistent with the caselaw. Given the many ways that incentives to compete can be affected by partial acquisitions, courts have not imposed a fixed, threshold percentage for determining when a transaction is illegal; they have simply looked at the likelihood of future anticompetitive effects. Much like the analysis in Areeda and Hovenkamp, judicial evaluations of substantial partial acquisitions have often led to the same conclusion that they may result in a substantial lessening of competition, just as a full acquisition would. Both the Supreme Court and lower courts have condemned partial acquisitions of 29% and lower.[1] In fact, plaintiffs are not aware of any case that has failed to treat a partial acquisition as if it were a full one when the defendant held 50% of the common and all of the preferred interests.

Given DFA's substantial holdings in both NDH and Southern Belle, those ownership interests, by themselves, make this a strong candidate for presumptive treatment as a full acquisition. But this conclusion is greatly strengthened when one adds to the picture the history of bid rigging, the close financial relationships between the executives involved (as described in section V below), how easy it is to reduce competition through market allocation, and the fact that all three players—DFA, Southern Belle, and Flav-O-Rich—have a unified interest in reducing competition.

[1] *See E.I. du Pont de Nemours*, 353 U.S. at 588 (finding illegal an acquisition of a 23% interest); *Crane Co. v. Briggs Mfg. Co.*, 280 F.2d 747, 748 (6th Cir. 1960)(per curiam) (finding illegal an acquisition of approx. 22% interest); *F&M Schaefer Corp. v. C. Schmidt & Sons*, 597 F.2d 814 (2d Cir. 1979) (29% illegal); *Navajo Terminals, Inc. v. United States*, 620 F.2d 594 (7th Cir. 1979) (26% sufficient so that transaction could be illegal); *Gulf & Western Indus., Inc. v. Great Atlantic & Pacific Tea Co.*, 476 F.2d 687 (2d Cir. 1973) (increasing ownership from over 4% to over 19% illegal); *Community Publishers Inc. v. Donrey Corp.*, 892 F. Supp. 1146, 1169 (W.D. Ark. 1995) (acquisition of 95% and 20% of two competitors was illegal); *Metro-Goldwyn-Mayer, Inc. v. Transamerica Corp.*, 303 F. Supp. 1344, 1345-46 (S.D.N.Y. 1969) (17% illegal); *American Crystal v. Cuban-Am. Sugar Co*, 152 F. Supp. 387, 392 (S.D.N.Y. 1957) (23% illegal); *Hamilton Watch Co. v. Benrus Watch Co.*, 114 F. Supp. 307 (D. Conn. 1953) (24% illegal).

IV. The defense fails because the transaction gives DFA an incentive and opportunity to reduce competition between Southern Belle and NDH, and because Southern Belle now has a greater incentive to avoid competing against NDH, another DFA dairy.

DFA obviously has an incentive to reduce competition between its dairies because DFA earns greater profits when the two dairies are collectively more profitable. But the transaction also reduces NDH's and Southern Belle's incentives to compete against each other. Both dairies will likely realize the benefits of pleasing their major stakeholder, DFA, and not harming the profitability of another DFA affiliate (and their own long-run profitability).

Throughout this litigation, DFA has repeatedly stressed that the United States has not proven that DFA has taken a specific act that raised a bid to a specific school district. This argument is insufficient for a number of reasons. First, the argument overlooks the transaction's effects on the dairies' incentives to compete less even without DFA's direct intervention.

Second, as noted previously, the Clayton Act employs an incipiency standard—a prediction about future possible effects is all that is required. It is hardly surprising that, while the government has been litigating this case, DFA has not taken overt steps to allocate markets, recorded those steps on paper, and turned over those incriminating documents to the government. The Supreme Court has long recognized, "If a demonstration that no anticompetitive effects had occurred at the time of trial or of judgment constituted a permissible defense to a § 7 divestiture suit, violators could stave off such actions merely by refraining from aggressive or anticompetitive behavior when such a suit was threatened or pending." *General Dynamics*, 415 U.S. at 504-05.

A third point—and one the Court need not consider in the present motion for partial summary judgment—is that plaintiffs will present at trial a statistical analysis of bid data since

DFA acquired Southern Belle, showing that, after controlling for influences on price other than competition, bids for school milk have already increased.

The greatest problem with DFA's argument is that the legality of a merger does not hinge on whether the government can prove that a transaction makes outright bid rigging more likely. Mergers are illegal if they may substantially reduce competition, and the potential reduction in competition may occur through a criminal conspiracy to rig bids, through tacit coordination between companies to bid less aggressively, or even through unilateral actions by one company to compete less against the other. "[W]e do not require a showing that the firms in the post-merger market actually intend to fix prices; we simply require proof that the market is more conducive to certain kinds of collusive or oligopoly behavior than it had been before." Herbert Hovenkamp, *Federal Antitrust Policy* at 498 (2d ed. 1999). Tacit coordination that does not constitute pricing fixing "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." *H.J. Heinz Co.*, 246 F.3d at 725 (quoting 4 Areeda, Hovenkamp & Solow, *Antitrust Law* ¶ 901b2, at 9 (rev. ed. 1998)).

The government therefore need not prove that DFA, Flav-O-Rich, and Southern Belle will all gather in a room one day and agree on the prices to charge for school milk, although that possibility cannot be ruled out. Less aggressive bidding of any sort between the two dairies would be sufficient. And a transaction in the most highly concentrated markets possible that further reduces the incentives for the dairies to compete against each other cannot help but create a reasonable probability that the dairies will compete less.

DFA has also argued that it will do nothing to reduce competition between Flav-O-Rich and Southern Belle because, in effect, the increased profits from reduced competition on school milk, estimated to be hundreds of thousands of dollars every year, simply aren't worth the trouble of obtaining them. But the argument overlooks that DFA is concerned about the profitability of its affiliates—even at the margins.

The uncontroverted discovery record shows that DFA works with its dairy affiliates to save money through a variety of means,

SF ¶ 45-61. Many of these projects involved small savings—

SF ¶ 46. The triviality of any one of these cost savings that DFA does become involved with belies DFA's claim that it would not care about hundreds of thousands of dollars in annual profits and that it will always remain uninvolved in the operation of its affiliates.

DFA does have an interest in reducing competition between the two dairies, and the modest effort required to facilitate reductions in competition would be worth more than many of the other matters in which DFA gets involved. More important, given DFA's common ownership in the two dairies, Flav-O-Rich and Southern Belle are highly unlikely to compete against each other, so DFA's intervention is unlikely to be necessary. DFA also obviously cannot argue that the dairies would have no interest in reducing competition between them, for the two dairies cared enough about those revenues to risk criminal prosecution and engage in bid rigging for a decade. A transaction that increases the incentives of these same dairies to reduce competition between them is itself illegal, regardless of direct involvement by DFA.

V. Cooperation short of bid rigging and even express collusion are made more likely because DFA's hand-picked partners are highly unlikely to compete against each other and cause financial losses to both themselves and DFA.

As noted above, cooperation and collusion are facilitated when companies in a market can rely on "mutual trust and forbearance" that eases "the temptation to steal a march on a fellow colluder by undercutting him slightly." *Hospital Corp. of America*, 807 F.2d at 1388. In assessing the likelihood of "mutual trust and forbearance," Judge Posner has noted the importance of "personal relations" between executives of competing companies. *See Antitrust Law* 78-79 (2d ed. 2001). *Cf. Arthur S. Langenderfer, Inc. v. S.E. Johnson Co.*, 729 F.2d 1050, 1056 n. 12 (6th Cir. 1984) (citing with approval the first edition of Judge Posner's book). Such personal relations can facilitate collusion because the "opportunities for communication thus created reduce the cost of collusion." *Id.* As an illustration, he cites the opportunities that executives in a regulated industry might have when meeting to lobby jointly for favorable legislation—an example of personal relations far more tepid than the connections and incentives here.

In this case DFA has a long history of friendly and mutually profitable financial dealings between it and the executives that it installed at the head of Southern Belle and NDH. DFA's first joint venture with the executive that DFA installed at the head of Southern Belle, Robert Allen, was the Lehigh Valley/Tuscan dairies. SF ¶ 18.

SF ¶ 19.

Although that transaction was highly profitable, the terms between DFA and Mr. Allen in setting up the next venture were even more remarkable.

Given the money that Mr. Allen has made with DFA, he has a substantial incentive to keep DFA happy so that he can continue to receive future profitable business opportunities, and

SF ¶

22. *Cf. Community Publishers Inc. v. Donrey Corp.*, 892 F. Supp. 1146, 1169 (W.D. Ark. 1995) (rejecting a "passive owner" defense where one family would own 95% of one newspaper and 20% of a competing paper; "the Stephens family members have little, if any, incentive to compete aggressively against themselves.").

The story is strikingly similar for Allen Meyer. Indeed, Mr. Meyer has made even more money with DFA than Mr. Allen.

VI. Any defense to a merger to monopoly (or duopoly) must be extraordinary.

Given the high market concentration in this case, DFA's defense faces an additional hurdle. Where a transaction reduces the number of competitors from two to one or from three to two, courts require an extraordinary showing to rebut the presumption of illegality, even without a history of bid rigging. For example, when faced with a merger that would reduce the number of competitors from three to two, with no history of collusion, the D.C. Circuit recently reversed the district court and rejected a defendant's argument that efficiencies produced by the transaction outweighed the presumption of illegality. "[T]he high market concentration levels present in this case require, in rebuttal, proof of extraordinary efficiencies, which the appellees failed to supply." *H.J. Heinz Co.*, 246 F.3d at 720. DFA's purported defense does not constitute "extraordinary" rebuttal evidence.

VII. The testimony by defendants' executives promising to compete and disclaiming any intent to exercise market power is legally irrelevant.

DFA has relied heavily on testimony from its executives asserting that they do not intend to lessen competition between the two dairies.

SF ¶

62. In other words, DFA implicitly acknowledges that it has the capacity to reduce competition; it just promises not to reap the benefits of that power. But promises of good behavior are insufficient, regardless of how sincerely made.

First, the Clayton Act does not include a *mens rea* requirement. The Supreme Court has specifically stated that, in merger cases under Section 7, it is "unnecessary for the Government to speculate as to what is in the 'back of the minds' of those who promote a merger." *Brown Shoe*, 370 U.S. at 329 n.48 (quoting H.R. Rep. No. 1191, 81st Cong., 1st Sess. 8). *See also E.I. du Pont de Nemours & Co.*, 353 U.S. at 589 (noting that Section 7 applies regardless of whether the substantial lessening of competition is "intended").

Second, and more generally, contemporary antitrust doctrine focuses on the rational incentives that companies have and seeks to avoid turning economic analysis into a more particularized, subjective psychological inquiry. This standard follows both from the fact that the Clayton Act requires only a "reasonable probability" of anticompetitive harm and from the general discounting of specific psychological intent as a measure of an antitrust violation. *See, e.g., Levine v. Central Florida Medical Affiliates, Inc.*, 72 F.3d 1538, 1552 (11th Cir. 1996); *U.S. Healthcare, Inc. v. Healthsource, Inc.*, 986 F.2d 589, 596 (1st Cir. 1993); *A.A. Poultry Farms, Inc. v. Rose Acre Farms, Inc.*, 881 F.2d 1396, 1402 (7th Cir. 1989); 1 Areeda and Hovenkamp *Antitrust Law* ¶ 113, at 137.

Courts do not assume that a business will act irrationally, refuse to exercise market power that a transaction has conferred on it, and forgo profits that could be easily obtained. *Cf. Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp.*, 475 U.S. 574, 596 (1986) (approving summary judgment against plaintiff's antitrust theory that assumed defendants would price below cost for twenty years without a reasonable hope of recovering those losses).

Areeda and Hovenkamp note, "As a general proposition business firms are (or must be assumed to be) profit maximizers, which means that they constructively 'intend' to take the course of action that maximizes their returns, given the physical and legal environment in which they find themselves." 1 *Antitrust Law* ¶ 113 at 134. A further illustration of this point is that the antitrust laws apply fully to nonprofit organizations, which are assumed to recognize and pursue their own rational self-interest as an organization. *See, e.g., NCAA v. Bd. of Regents of the Univ. of Oklahoma*, 468 U.S. 85, 100-01 n.22 (1984); *Hospital Corp. of America,* 807 F.2d at 1390.

Courts' refusal to rely on statements of intent by executives is further supported by the fact that business leadership and intent can quickly change, while mergers and their competitive effects can last long into the future. Indeed, in this case, DFA is already grooming a successor to Gary Hanman. SF ¶ 68.

The Sixth Circuit has also rejected a defense much like DFA's in a market far less concentrated and susceptible to coordination than this one. In *Crane Co. v. Briggs Mfrg. Co.*, 280 F.2d 747 (6th Cir. 1960) (*per curiam*), the defendant, Crane, purchased approximately 22% of the outstanding shares of Briggs's voting common stock, making Crane the largest shareholder of Briggs. Crane then submitted seven nominees for the board of Briggs. In opposing an injunction under the Clayton Act seeking to block the acquisition, Crane had each of its seven nominees file "an affidavit stating that they would act as an impartial and independent director, serving the best interests of Briggs and would not be responsible in any manner to Crane." 280 F.2d at 749.

The Sixth Circuit squarely rejected the defense, noting that the Crane nominees' presence on Briggs's board would create a "'listening line' which Crane would have in Briggs." *Id.* at 750. The court continued:

> As Chief Judge Levin stated "since the two companies are competitors, the Briggs Board would be unable to perform its proper functions in connection with the management of the company without divulging to a competitor confidential information with respect to the development of processes and techniques; plans for improvement of products and plans for sales and promotion campaigns."

Id. at 750 (quoting *Briggs Mfrg. Co. v. Crane Co.*, 185 F. Supp. 177, 181 (E.D. Mich. 1960)).

Significantly, when the district court in *Crane* concluded that the seven nominees' affidavits were insufficient, the court expressly stated that "I have no reason to doubt the integrity of the Crane nominees." 185 F. Supp. at 181. And no credibility judgments could have been made, for the court made its ruling based solely on affidavits and exhibits. 185 F. Supp. at 179. This holding makes eminent sense given the Supreme Court's conclusion that the Clayton Act does not include a *mens rea* requirement, given that courts shun intent evidence in favor of an objective assessment of what rational actors in the market would do, and given that the Clayton Act requires only a reasonable probability of anticompetitive effects.

Conclusion

Through its substantial investments in both NDH and Southern Belle, DFA has an interest in seeing the two dairies compete less, for the dairies will be more profitable and hence DFA's returns will be greater. The dairies also have an incentive not to harm another DFA affiliate, undermining their own long-run profitability. Given that DFA carefully selected the joint venture partners, they are more likely to avoid damaging outbreaks of competition. They have a long and close history of highly profitable dealings with each other; they trust one another; and they hope to complete more deals in the future. These are facts far more extreme than those the Sixth Circuit found wanting in *Crane*. The market itself is also as concentrated as any possible in antitrust analysis, and there is a history of bid rigging, two factors that call for extraordinary rebuttal evidence to demonstrate that a transaction poses no reasonable probability of anticompetitive harm.

The defendants have also given this Court little reason to risk allowing a single company to install its long-time business partners as the only two competitors in a highly concentrated market with a history of bid rigging. DFA has alleged no efficiencies from this transaction, but in the absence of merger-specific efficiencies, there is no reason to approve an acquisition in a highly concentrated market susceptible to anticompetitive harm. *See, e.g., H.J. Heinz Co.*, 246 F.3d at 720. Put differently, DFA can achieve whatever investment opportunities that it hopes to gain by purchasing another dairy—one not located thirty miles from its competitor, in a market as susceptible to coordination and collusion as this one is. The probability of anticompetitive harm that courts presume from a merger to monopoly of two former bid riggers is not negated when the parent holds "only" 50% of the equity and all of the preferred interests. Indeed, courts have routinely treated partial acquisitions the same as full acquisition at much lower levels of ownership and in markets far less susceptible to anticompetitive effects.

For the foregoing reasons, the United States and the Commonwealth of Kentucky should be granted partial summary judgment on DFA's "control" affirmative defense.

Respectfully submitted,

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