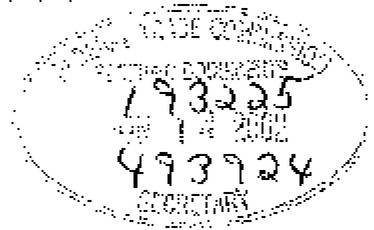


UNITED STATES OF AMERICA
BEFORE THE FEDERAL TRADE COMMISSION

In the Matter of	)	
	)	Docket No. 9299
MSC.SOFTWARE CORPORATION, a corporation.	)	

COMPLAINT COUNSEL'S PRE-TRIAL PROPOSED CONCLUSIONS OF LAW

I. THE STANDARD FOR FINDING A VIOLATION OF SECTION 7 AND SECTION 5 IS MET

1. Clayton Act § 7, 15 U.S.C. § 18, prohibits mergers or acquisitions of "the whole or any part of the stock . . . [or] the whole or any part of the assets of another person . . ., 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." As the Supreme Court held in its first case considering the statute (as rewritten by the Celler-Kefauver Amendments of 1950, 64 Stat. 1225),

> Section 7 is designed to arrest in its incipiency not only the substantial lessening of competition from the acquisition by one corporation of the whole or any part of the stock of a competing corporation, but also to arrest in their incipiency restraints or monopolies in a relevant market which, as a reasonable probability, appear at the time of suit likely to result at the time of the acquisition by one corporation of all or any part of the stock of any other corporation.

United States v. E.I. du Pont de Nemours & Co., 353 U.S. 586, 589, 77 S. Ct. 872, 875 (1957).

2. The Supreme Court has held that Section 7 "creates a relatively expansive definition of antitrust liability" regarding mergers and acquisitions. *California v. American Stores Co.*, 495 U.S. 271, 284, 110 S. Ct. 1853, 1860 (1990).

3. Under Section 7, Complaint Counsel make out a *prima facie* case giving rise to a

presumption of violation by showing: (1) the "line of commerce" or product market; (2) the "section of the country" or geographic market; and (3) the transaction's probable effect on concentration in the product and geographic markets. *Federal Trade Comm'n v. H.J. Heinz Co.*, 246 F.3d 708, 715 (D.C. Cir. 2001); *Federal Trade Comm'n v. University Health, Inc.*, 938 F.2d 1206, 1218 (11th Cir. 1991); *United States v. Baker Hughes, Inc.*, 908 F.2d 981, 982-83 (D.C. Cir. 1990); *Federal Trade Comm'n v. Warner Communications*, 742 F.2d 1156, 1160 (9th Cir. 1984); *Federal Trade Comm'n v. Swedish Match*, 131 F. Supp. 2d 151, 156 (D.D.C. 2000); *Federal Trade Comm'n v. Cardinal Health, Inc.*, 12 F. Supp. 2d 34, 52 (D.D.C. 1998).

4. Courts have regularly confirmed that the reliability of market concentration as proof of the plaintiff's *prima facie* case, and held that defendants, not the government, must prove that a merger that substantially increases market concentration nonetheless would not result in a substantial loss of competition. *Heinz*, 246 F.3d at 715; *accord Baker Hughes*, 908 F.2d at 982-83; *United States v. Rockford Mem. Corp.*, 898 F.2d 1278, 1285-86 (7th Cir.) ("once the government showed that the merger would create a firm having a market share approaching, perhaps exceeding, a common threshold of monopoly power – two-thirds – it behooved the defendants *to present evidence* that the normal inference to be drawn from such a market share would mislead"), *cert. denied*, 498 U.S. 920, 111 S. Ct. 295 (1990); *Swedish Match*, 131 F. Supp. 2d at 167; *Cardinal Health*, 12 F. Supp. 2d at 54. In order "to meet this burden, the defendants must show that the market share statistics 'give an inaccurate prediction of the proposed acquisition's probable effect on competition.'" *Swedish Match*, 131 F. Supp. 2d at 167 (quoting *Federal Trade Comm'n v. Staples, Inc.*, 970 F. Supp. 1066, 1083 (D.D.C. 1997)); *accord Allied Signal, Inc. v. B.F. Goodrich Co.*, 183 F.3d 568, 574-75 (7th Cir. 1999) (rejecting defendants' "power buyer" argument); *Baker Hughes*, 908 F.2d at 991; *see generally Hospital*

Corp. of America v. Federal Trade Comm'n, 807 F.2d 1381, 1388 (7th Cir. 1986) (FTC's "showing that the challenged acquisitions gave four firms control over an entire market . . . went far to justify its prediction of probable anticompetitive effects"), *cert. denied*, 481 U.S. 1038, 107 S. Ct. 1975 (1987). High levels of concentration establish a strong *prima facie* case. "[T]he more compelling the *prima facie* case, the more evidence the defendant must present to rebut it successfully." *Heinz*, 246 F.3d at 725 (quoting *Baker Hughes*, 908 F.2d at 991).

5. "To meet their burden, the defendants must show that the market-share statistics . . . 'give an inaccurate prediction of the proposed acquisition's probable effect on competition.'" *Cardinal*, 12 F. Supp. 2d at 54 (quoting Staples, 970 F. Supp. at 1083); *accord United States v. Citizens & Southern Nat'l Bank*, 422 U.S. 86, 120, 95 S. Ct. 2099, 2118 (1975); *United States v. Marine Bancorporation*, 418 U.S. 602, 631, 94 S. Ct. 2856, 2874 (1974); *Baker Hughes*, 908 F.2d at 991. If the defendant comes forward with evidence sufficient to rebut the presumption, the burden of producing further evidence of anticompetitive effect shifts to the government, which retains the burden of proof at all times. *Baker Hughes*, 908 F.2d at 982-83; *Cardinal Health*, 12 F. Supp. 2d at 54; *United States v. Ivaco, Inc.*, 704 F. Supp. 1409, 1420-21 (W.D. Mich. 1989).

6. In proscribing mergers that "may . . . substantially lessen competition, or tend to create a monopoly," Congress used the words "may be" to "indicate that its concern was with probabilities, not certainties." *Brown Shoe Co. v. United States*, 370 U.S. 294, 323, 82 S. Ct. 1502, 1522 (1962). Thus, the Supreme Court reaffirmed in *American Stores* that "plaintiff need only prove that [the challenged acquisition's] effect '*may be* substantially to lessen competition.'" 495 U.S. at 284, 110 S. Ct. at 1860 (emphasis in original).

7. It follows from Section 7's incipiency standard that the statute "does not require

proof that a merger or other acquisition has caused higher prices in the affected market. 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; *see id.* at 713 (discussing legislative history); *Hospital Corp.*, 807 F.2d at 1389. Section 7 does not require "a certainty, or even a high probability," that an acquisition will substantially lessen competition. *Elders Grain*, 868 F.2d at 906. "[D]oubts are to be resolved against the transaction." *Id.* To satisfy Section 7, the government need only show "a reasonable probability that the proposed transaction would substantially lessen competition in the future." *University Health, Inc.*, 938 F.2d at 1218.

IV. ADVANCED NASTRAN IS A RELEVANT PRODUCT MARKET

8. The goal of merger analysis is to determine whether a merger is likely to reduce competition in a manner that would increase the risk of market power, *i.e.*, the ability of the merged firm profitably to raise price (alone or in concert with competitors). *Merger Guidelines* § 0.1. "Congress neither adopted nor rejected specifically any particular tests for measuring the relevant markets, either as defined in terms of product or in terms of geographic locus of competition, within which the anticompetitive effects of a merger were to be judged." *Brown Shoe,* 370 U.S. at 320-21, 82 S. Ct. at 1521. Modern merger policy and merger law focuses on "the unifying theme . . . that mergers should not be permitted to create or enhance market power or facilitate its exercise." *Merger Guidelines* § 0.1[1]; *see United States v. Archer-Daniels-Midland Co.*, 866 F.2d 242, 246 (8th Cir. 1988), *cert. denied*, 493 U.S. 809, 110 S. Ct. 51 (1989). Professor Fisher explains the concept of constraint, as applied to product market definition (in

---

[1] "Market power to a seller is the ability profitably to maintain prices above competitive levels for a significant period of time." *Id.*

the context of monopolization cases), as follows:

> The conventional first step in analyzing whether a given firm does or does not have monopoly power is to define the relevant market in which the alleged power is exercised. Unfortunately, this is not as simple as it sounds and tends to lead to confusion, if not abuse. . . .
>
> Let us begin by recalling what the purpose is of market definition. It is the beginning of an analysis of monopoly power. Monopoly power, however, is the ability to act in an unconstrained way. Hence, market definition, if it is to be an aid to analysis, has to place in the relevant market those products and services and firms whose presence and actions can serve as a constraint on the policies of the alleged monopolist. . . .
>
> Thus, the primary question in defining a relevant market ought to be that of the constraints on the alleged monopolist. . . . The courts have paid appropriate attention to demand and supply substitutability – appropriate because those are the criteria by which to judge the constraints on the alleged monopolist. It should not be forgotten, however, that *it is the constraints which are the object of analysis and not the properties of substitutability themselves.*

F. Fisher, *Industrial Organization, Economics and the Law* 9-10 (1991) (emphasis added). Product market definition advances the goal of identifying mergers that threaten competition by identifying a relevant group of competitors, *i.e.*, those competitors that *would plausibly constrain* the exercise of market power. Only by identifying relevant, effective, constraining competitors can the court determine whether those competitors will prevent the merger from impairing competition.

9. "The *outer boundaries* of a product market are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it." *Brown Shoe*, 370 U.S. at 325, 82 S. Ct. at 1523-1524 (emphasis added). "Reasonable interchangeability" and "cross-elasticity of demand" are distinct concepts. *Staples*, 970 F. Supp. at 1074. "Reasonable interchangeability" asks whether products or services perform the same function. "Cross-elasticity of demand" asks whether demand for one product

is affected by the price of the other product, and seeks to determine whether customers would in fact substitute one for the other in the event of small changes in price. *Id.*

10. "Reasonable interchangeability" defines the *outer bounds* of the product market, not the narrowest product market -- which is defined by identifying the products to which customers would switch (*i.e.*, the "cross-elasticity of demand" for the product). *Brown Shoe*, 370 U.S. at 325, 82 S. Ct. at 1523-24; *Allen-Myland, Inc. v. International Business Machines Corp.*, 33 F.3d 194, 206 (3d Cir.), *cert. denied*, 513 U.S. 1066, 115 S. Ct. 684 (1994).

11. Within the broad range of "reasonably interchangeable" products, "well-defined submarkets may exist which, in themselves, *constitute product markets for antitrust purposes.*" *Brown Shoe*, 370 U.S. at 325, 82 S. Ct. at 1524 (citing *United States v. E.I. du Pont de Nemours & Co.*, 353 U.S. 586, 593-95, 77 S. Ct. 872, 877-878 (1956)); *see Staples*, 970 F. Supp. at 1075-81 (finding submarket of office supply superstores within broader market of sale of office supplies).

12. Reasonable interchangeability alone, *i.e.*, the fact that some products may superficially (or even on careful examination) appear to be similar in use, or have similar "attributes," does not warrant including a purportedly interchangeable substitute in the product market. "Functional interchangeability," *i.e.*, whether products are similar in character and use, defines the outer bounds of the product market, not the product market itself. "[T]he Supreme Court did not stop after finding a high degree of functional interchangeability" in *du Pont*, 351 U.S. at 400, 76 S. Ct. at 1010, and the court did not stop with functional interchangeability in *Staples*, even though identical office supplies could be purchased through vendors other than the merging office supply superstore chains. 970 F. Supp. at 1074 (quoting 351 U.S. at 400, 76 S. Ct. at 1010).

13. Reliance on functional interchangeability alone can result in significant market definition error, *e.g.*, the inclusion of all methods of transportation (cars, bicycles, feet) when evaluating a merger of Ford and General Motors. *Allen-Myland*, 33 F.3d at 206. "The key test for determining whether one product is a substitute for another is whether there is a cross-elasticity of demand between them: in other words, whether the demand for the second good would respond to changes in the price of the first." *Id.*

14. Products that are "reasonably interchangeable" may be in different antitrust markets because of the price disparity between the two products. For example, the Supreme Court found that aluminum cable constituted a distinct submarket from copper cable (and therefore a distinct market for Clayton Act purposes), even though "each does the job equally well," in light of the fact that copper cable was 50% more expensive than aluminum cable. *United States* v. *Aluminum Co. of America*, 377 U.S. 271, 276-77, 84 S. Ct. 1283, 1287 (1964) ("[H]ere, where insulated aluminum conductor pricewise stands so distinctly apart, to ignore price in determining the relevant line of commerce is to ignore the single, most important, practical factor of the business").

15. It is insufficient that another product is *in some sense* an alternative, if the product is not one that consumers would turn to in response to price changes -- and therefore not one that would constrain price increases following the merger. The relevant product market "must be drawn narrowly to exclude any other product to which, within reasonable variations in price, only a limited number of buyers will turn." *Times-Picayune Publishing Co. v. United States*, 345 U.S. 594, 612 n.31, 73 S. Ct. 872, 883 n.31 (1953); *Merger Guidelines* § 1.11 ("the Agency will begin with each product (narrowly defined) produced or sold by each merging firm and ask what would happen if a hypothetical monopolist of that product imposed at least a 'small but significant and

nontransitory' increase in price," adding products only until such a price increase would be profitable). As Areeda puts it:

> the "line of commerce" language of § 7 of the Clayton Act and the general principles of merger policy require the government to identify *some* grouping of sales that constitutes a relevant market in which prices might rise as a consequence of the merger. That a larger group of sales might also constitute a market is beside the point.

4 P. Areeda, H. Hovenkamp & J. Solow, *Antitrust Law* (rev. ed. 1998) (hereafter "Areeda") ¶ 929d, at 130.

16. In *Swedish Match,* 131 F. Supp. 2d at 164, the court found that "moist snuff competes with loose leaf [chewing tobacco] to a limited degree," but nonetheless *excluded* loose leaf from the product market:

> But there is ultimately an insufficient amount of evidence to convince the Court that moist snuff induces an adequate level of substitution *to constrain* loose leaf prices. To the contrary, the weight of the evidence demonstrates that moist snuff *is incapable of inducing substitution sufficient enough to render loose leaf price increases unprofitable* and cannot, therefore, be included in the relevant market on this basis.

*Swedish Match,*131 F. Supp. 2d at 164 (emphasis added). *See generally* 4 Areeda ¶ 929d, at 127-33 (discussing market definition examples of electric saws versus electric and hand saws, and personal computers versus personal computers and workstations); F. Scherer & D. Ross, *Industrial Market Structure & Economic Performance* 180-81 (3d ed. 1990) (discussing glass and plastic containers).

17. "[I]t is ordinarily quite difficult to measure cross-elasticities of supply and demand accurately. Therefore, it is usually necessary to consider other factors that can serve as useful surrogates for cross-elasticity data." *United States Anchor Mfg., Inc. v. Rule Indus., Inc.*, 7 F.3d 986, 995 (11th Cir. 1993) (quoting *International Tel. & Tel. Co.*, 104 F.T.C. 280, 409

(1984)). Since it is ordinarily quite difficult to measure cross-elasticity (or own-elasticity) directly, there is no burden on the Complaint Counsel to do so. *Swedish Match*, 131 F. Supp. 2d at 162-63.

18. Because it is usually difficult to measure cross-elasticities of demand, courts also have identified "practical indicia" of product market boundaries, such as

> industry or public recognition of the submarket [or market] as a separate economic entity, the product's particular characteristics and uses, unique production facilities, distinct customers, sensitivity to price changes, and specialized vendors.

Brown Shoe, 370 U.S. at 325, 82 S. Ct. at 1524; *see also Cardinal Health*, 12 F. Supp. 2d at 46; *Staples*, 970 F. Supp. at 1075; *Federal Trade Comm'n v. Coca-Cola Co.*, 641 F. Supp. 1128, 1133 (D.D.C. 1986) (citing cases), *vacated as moot*, 829 F.2d 191 (D.C. Cir. 1987). These "practical indicia" are "evidentiary proxies for direct proof of substitutability" among products. *Rothery Storage & Van Co. v. Atlas Van Lines*, 792 F.2d 210, 218 (D.C. Cir. 1986).

19. Customers' perceptions of the marketplace, the defendants' documents reflecting the "business reality" of "how the market is perceived by those who strive to profit in it," and industry or public perception of separate markets are highly probative of the boundaries of the relevant market. *Coca-Cola*, 641 F. Supp. at 1132; *see Swedish Match*, 131 F. Supp. 2d at 161-62 (customer and competitor testimony, and defendants' business documents, found more persuasive than expert testimony); *Cardinal Health, Inc.*, 12 F. Supp. 2d at 49, 63-64; *Staples*, 970 F. Supp. at 1089; *Olin Corp. v. Federal Trade Comm'n*, 986 F.2d 1295, 1299 (9th Cir. 1993), *cert. denied*, 510 U.S. 1110, 114 S. Ct. 1051 (1994); *Rothery*, 792 F.2d at 218 n.4 ("industry or public recognition of the [submarket] as a separate economic unit matters because we assume that economic actors usually have accurate perceptions of economic realities").

Under the principles discussed above, Respondent's business documents reflect that advanced Nastran is a separate antitrust market. Respondent developed distinct sales strategies for advanced Nastran, and evaluated pricing and profitability separately for advanced Nastran. Users also believe that advance Nastran is a separate market. Those documents are far more probative of the "business reality" of this market than is the self-serving testimony of Respondent's businessmen and consultants

20. In defining markets, the finder of fact should look at all available evidence, including in particular the "ordinary course of business" documents of the merging parties, *e.g.*, *Warner*, 742 F.2d at 1163 ("record company documents"); *Cardinal*, 12 F. Supp. 2d at 49; *Staples*, 970 F. Supp. at 1076; *In the Matter of Olin Corp.*, 113 F.T.C. 400, 597 (1990), *aff'd sub nom. Olin Corp. v. Federal Trade Comm'n*, 986 F.2d 1295 (9th Cir. 1993), *cert. denied*, 510 U.S. 1110, 114 S. Ct. 1051 (1994); and on the testimony of competitors and customers (including intermediate purchasers such as retailers), *e.g.*, *Federal Trade Comm'n v. PPG Industries, Inc.*, 798 F.2d 1500, 1504 (D.C. Cir. 1986) ("buyers' and sellers' perceptions"); *Warner*, 742 F.2d at 1163; *Borden v. Federal Trade Comm'n*, 674 F.2d 498, 507-08 (6th Cir. 1982) ("buyers for large supermarket chains and representatives of processed lemon juice companies"), *vacated on other grounds*, 461 U.S. 940 (1983).

21. Documents prepared for any corporate officer or director for the purpose of evaluating or analyzing a proposed acquisition or transaction are especially probative. *See* Federal Trade Commission, Premerger Notification Rules, 16 C.F.R. § 803.1 & App. Such documents that analyze the acquisition with respect to market shares, competition, competitors, markets, potential for sales growth or expansion into product or geographic markets are highly relevant for merger review. *Id.*

22. The antitrust agencies and the courts often approximate the ultimate question of constraint by seeking to identify alternatives to which consumers likely would turn in the event of a small price increase. "A market is the set of sellers to which a set of buyers can turn for supplies *at existing or slightly higher prices*." *Elders Grain, Inc.*, 868 F.2d at 907 (emphasis added). Market definition is an exercise to distinguish close competitive constraints from distant ones, so that the analysis can then proceed to examine whether the merger significantly reduces competition among *close* constraints. *See, e.g.*, 4 Areeda, ¶ 929c. The antitrust agencies and the courts have implemented these tests by seeking to identify the smallest group of products over which prices could be profitably increased by a "small but significant" amount (normally 5%) for a substantial period of time (normally one year). *Staples*, 970 F. Supp. at 1076 n.8; *Merger Guidelines* § 1.11.

23. One surrogate for cross-elasticity data is the "hypothetical monopolist" test, *i.e.*, to examine whether customers would switch to other products in response to a hypothesized small but significant, non-transitory increase in price ("SSNIP") for the products of a hypothetical monopolist consisting of the merging firms and all other firms to which customers would switch. *Merger Guidelines* § 1.11; *see, e.g.*, *Olin Corp.*, 986 F.2d at 1301-03 (adopting and applying "5% test"). If advanced Nastran users would not reduce usage by an amount sufficient to make the price increase unprofitable, the market is established. *Merger Guidelines* § 1.11.

24. The "hypothetical monopolist" or "5% test" cannot normally be applied with mathematical precision. "Although the antitrust enforcement agencies attempt to apply this hypothetical monopolist test, most often, the data simply is not there to do so." ABA Section of Antitrust Law, *Mergers and Acquisitions: Understanding the Antitrust Issues* 48-49 (2000). Therefore, the *Merger Guidelines* themselves state:

> In considering the likely reaction of buyers to a price increase, the Agency will take into account all relevant evidence, including, but not limited to, the following:
>
> > (1) evidence that buyers have shifted or have considered shifting purchases between products in response to relative changes in price or other competitive variables;
> >
> > (2) evidence that sellers base business decisions on the prospect of buyer substitution between products in response to relative changes in price or other competitive variables . . . .

Merger Guidelines § 1.0. There is no requirement in the *Guidelines* or in the law that the government show (either on application for a preliminary injunction or at trial on the merits) precisely how many consumers would or would not substitute what products in response to a 5% price increase.

25. However, another product is not necessarily in the same product market simply because consumers consider it to be a viable substitute at prevailing prices. To make such an assumption is to fall victim to the "Cellophane Fallacy." *See, e.g.*, *United States v. Eastman Kodak Co.*, 63 F.3d 95, 103 (2d Cir. 1995) ("[A] monopolist . . . always faces a highly elastic demand; its products are so overpriced that even inferior substitutes begin to look good to consumers."); *Pepsico, Inc. v. The Coca Cola Co.*, 114 F. Supp. 2d 243, 257 (S.D.N.Y. 2000) (the Cellophane Fallacy "cautions that '[the] existence of significant substitution in the event of further price increases or even at the current price does not tell us whether the defendant already exercises significant market power.'" (quoting *Eastman Kodak Co. v. Image Tech. Serv. Inc.*, 504 U.S. 451, 471 (1992))); *see also Santa Cruz Medical Clinic v. Dominican Santa Cruz Hospital*, No. C93-20613-RMW, 1995 WL 853037, at *10 & n.10 (N.D. Cal., Sept. 7, 1995) (discussing Cellophane Fallacy in context of geographic market definition) (citing Gene C. Schaerr, *The Cellophane Fallacy and the Justice Department's Guidelines for Horizontal Mergers*, 94 Yale

L.J. 670, 677-78 (1984)).

26. MSC is an Advanced Nastran monopolist and can profitably impose at least a small but significant increase in price for a nontransitory period of time (one year). PFF 35, 39, 75, 147. The test considers a "hypothetical monopolist" in order to separate the effect of competition *within* the hypothesized product market from competition from products and suppliers *outside* the hypothesized product market.

27. The relevant market should be defined on the basis of competitive conditions as they existed at the time of the acquisition. *See In the Matter of R.R. Donnelley & Sons Co.*, 120 F.T.C. 36, 153 (1995) (considering market conditions at time of allegedly unlawful merger); *see also United States v. General Dynamics Corp.*, 415 U.S. 486, 504-05 (1974) (disregarding evidence of market conditions after transaction had been completed); *Hospital Corp. of Am.*, 807 F.2d at 1384 (same).

28. Advanced Nastran is not part of an antitrust "cluster market" consisting of product commonly sold or transacted for together. Finding a "cluster market" consisting of a bundle of putatively related goods is not appropriate except where "industry generally considers it necessary to carry a full line [of those products], and advertising and promotion often group the products." *JBL Enterprises, Inc. v. Jhirmack Enterprises, Inc.*, 698 F.2d 1011, 1017 (9th Cir. 1983), *cert. denied*, 464 U.S. 829 (1983). Accordingly, the "cluster approach is appropriate where the product package is significantly different from, and appeals to buyers on a different basis from, the individual products considered separately." *Id.* at 1016-17. Where consumers do not have a particular demand for the purchase of products together, then a cluster market is not appropriate. *Thurman Industries, Inc. v. Pay 'n Pak Stores, Inc.*, 875 F.2d 1369, 1377 (9th Cir. 1989).

29. Advanced Nastran constitutes a relevant product market under the antitrust laws and a "line of commerce" within the meaning of Clayton Act § 7.

V. THE RELEVANT GEOGRAPHIC MARKET IS AS BROAD AS THE WORLD, AND NO NARROWER THAN THE UNITED STATES.

30. The relevant geographic market is that area beyond which a customer could not practically turn for an alternative supplier. *Morgenstern v. Wilson*, 29 F.3d 1291, 1296 (8th Cir. 1994) (a geographic market is that geographic area "to which consumers can practically turn for alternative sources of the product and in which the antitrust defendant faces competition."); *Staples*, 970 F. Supp. at 1073 (same).

31. In this matter, the world or the United States constitutes the relevant geographic market within the meaning of the antitrust laws and a "section of the country" within the meaning of Section 7 of the Clayton Act.

VI. ACTUAL ANTICOMPETITIVE EFFECTS CAN SHORTEN THE MARKET DEFINITION INQUIRY

32. Evidence of actual anticompetitive effects—such as price increases or output reductions—can obviate extensive inquiry into market definition. *Federal Trade Comm'n v. Indiana Federation of Dentists*, 476 U.S. 447, 460-61 (1986); *accord Toys 'R' Us, Inc. v. Federal Trade Comm'n*, 221 F.3d 924, 937 (market power may be proven through evidence of anticompetitive effects or proof of relevant markets and market concentrations above the relevant threshold); *Federal Trade Comm'n v. Libbey, Inc.*, No. 02-CV-60, 2002 WL 984208, at *10 (D.D.C., Apr. 22, 2002) (where Commission can show after administrative investigation that there were "actual sustained adverse effects on competition" then it need not engage in elaborate market analysis).

33. "[P]ost-acquisition evidence that is subject to manipulation by the party seeking to

use it is entitled to little or no weight." *Hospital Corp. of America*, 807 F.2d at 1384. Accordingly, the "Commission . . . was not required to take account of a post-acquisition transaction that may have been made to improve [defendant's] litigating position." *Id.*; *see B.F. Goodrich Co.*, 110 F.T.C. 207, 340-41 (1988) ("performance evidence must be evaluated very carefully, because of its potential for manipulation. . . . the Commission has determined that it is inappropriate to consider 'exculpatory post-acquisition evidence of voluntary actions by the acquiring firm' in determining the legality of an acquisition.'").

34. "If the post-acquisition evidence were given conclusive weight or allowed to override all probabilities, the acquisitions would go forward willy-nilly, the parties biding their time until reciprocity was allowed fully to bloom." *Federal Trade Comm'n v. Consolidated Foods*, 380 U.S. 592, 598 (1965); *General Dynamics*, 415 U.S. at 504-05 ("If a demonstration that no anticompetitive effects had occurred at the time of trial or of judgment constituted a permissible defense to a sec. 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.").

VI. THERE IS A SUBSTANTIAL LIKELIHOOD THE ACQUISITIONS MAY LESSEN COMPETITION IN VIOLATION OF SECTION 7 OF THE CLAYTON ACT

35. A merger that results in a significant increase in concentration, and produces a firm that has an undue percentage share of the 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." *Swedish Match*, 131 F. Supp. 2d at 166, (quoting *Philadelphia Nat'l Bank*, 374 U.S. at 363, 83 S. Ct. at 1741); *accord Heinz*, 246 F.3d at 715. Therefore, "sufficiently large HHI figures establish the FTC's *prima facie* case

that a merger is anticompetitive." *Heinz*, 246 F.3d at 716, (citing *Philadelphia Nat'l Bank*, 374 U.S. at 363, 83 S. Ct. at 1741); *accord Baker Hughes*, 908 F.2d at 982; *see Swedish Match*, 131 F. Supp. 2d at 168 (describing the "anticompetitive behavior already exhibited within the market" and concluding "this pattern of anticompetitive behavior stems from high concentration in the market, and the defendants have not adequately demonstrated that competition will be facilitated by increasing that concentration"). These acquisitions have given MSC a monopoly, far exceeding the level that has been held to be presumptively unlawful.

36. "[M]arket share, which companies may control by merging, is one of the most important factors to be considered" when analyzing the likely effects of a merger. *Brown Shoe*, 370 U.S. at 343, 82 S. Ct. at 1534; *see Cardinal Health*, 12 F. Supp. 2d at 52. A merger that significantly increases market shares and market concentration beyond already high levels is so inherently likely to lessen competition substantially that it is presumptively unlawful under Section 7 of the Clayton Act. *Philadelphia Nat'l Bank*, 374 U.S. at 363, 83 S. Ct. at 1741; *Baker Hughes*, 908 F.2d at 982-83; *PPG*, 798 F.2d at 1502-03.

37. Market concentration should be measured using the Herfindahl-Hirschman Index ("HHI"), as adopted by the Commission. *Merger Guidelines* § 1.5. Courts have also adopted and relied on the HHI as a measure of market concentration. *E.g., PPG*, 798 F.2d at 1503; *University Health*, 938 F.2d at 1211 n.12 (HHI is "most prominent method" of measuring market concentration); *Staples*, 970 F. Supp. at 1081-82; *Cardinal Health*, 12 F. Supp. 2d at 53-54; *United States v. Ivaco*, 704 F. Supp. 1409, 1419 (W.D. Mich. 1989). The HHI is calculated by summing the squares of the market shares of all firms in the market. An HHI over 1800 (post-merger) indicates a highly concentrated market, and an HHI increase of more than 100 is a sufficiently significant increase in concentration to give rise to the *Philadelphia Nat'l Bank*

presumption. *Merger Guidelines* § 1.51(c).

38. A merger or acquisition that significantly increases market shares and concentration to high levels creates a presumption that the merger is illegal under Section 7 of the Clayton Act. *Philadelphia Nat'l Bank*, 374 U.S. at 363, 83 S. Ct. at 1741; *Baker, Hughes*, 908 F.2d at 982-83 (D.C. Cir. 1990); *PPG*, 798 F.2d at 1502-03; *Cardinal Health*, 12 F. Supp. 2d at 52.

39. Mergers resulting in substantially lower concentration levels than here are regularly blocked. *Elders Grain*, 868 F.2d at 902 (acquisition increased market shares of largest firm from 23% to 32%); *Hospital Corp.*, 807 F.2d at 1384 (acquisition increased market share of second largest firm from 14% to 26%); *Warner Communications*, 742 F.2d at 1163 (acquisition increased market share of second largest firm from 19% to 26%; four-firm concentration ratio of 75%); *Cardinal Health*, 12 F. Supp. 2d at 52 (mergers increasing HHIs from 1648 to 2450 and from 1648 to 2277; increasing market shares from 25% to 37% and from 22% to 40%); *United States v. United Tote, Inc.*, 768 F. Supp. 1064, 1069-70 (D. Del. 1991) (merger between second and third largest firms in 3-firm market with 13% and 27% of sales, increasing the HHI from 3940 to 4640, held presumptively unlawful); *Federal Trade Comm'n v. Bass Bros. Enters., Inc.*, 1984-1 Trade Cas. (CCH) ¶ 66,041, at 68,609-10 (N.D. Ohio 1984) (acquisition increased market share of second largest firm from 20.9% to 28.5%, increasing HHI from 1802 to 2320).

40. Since the FTC has proven that the acquisition would significantly increase concentration in one or more relevant product markets in the world and the United States, the acquisition is presumed to violate the Clayton Act. *Philadelphia Nat'l Bank*, 374 U.S. at 363, 83 S. Ct. at 1741-1742; *Baker Hughes*, 908 F.2d at 982; *Cardinal Health*, 12 F. Supp. 2d at 52 ("under Section 7 of the Clayton Act, a *prima facie* case can be made if the government

establishes that the merged entities will have a significant percentage of the relevant market–enabling them to raise prices above competitive levels").

41. The Supreme Court explained the rationale for this principle in *United States v. General Dynamics Corp.*, 415 U.S. 486, 497, 94 S. Ct. 1186, 1194 (1974):

> The effect of adopting this approach to a determination of a "substantial" lessening of competition is to allow the Government to rest its case on a showing of even small increases of market share or market concentration in those industries or markets where concentration is already great or has been recently increasing, since "if concentration is already great, the importance of preventing even slight increases in concentration is correspondingly great." *Alcoa*, 377 U.S. at 279, 84 S. Ct. 1283, 1289, *citing Philadelphia National Bank*, 374 U.S. at 365, n.42, 835 S. Ct. 1715, 1743 n.42.

VII. THERE IS NO EVIDENCE TO REBUT THE PRESUMPTION OF LIKELY ANTICOMPETITIVE EFFECTS OF THE MERGER

42. By proving that the acquisition will increase concentration significantly in the advanced Nastran market, the Commission establishes its *prima facie* case that a merger is anticompetitive. *Heinz*, 246 F.3d at 716 (*prima facie* case demonstrated by showing that market concentration would increase substantially). The burden of production and proof shifts to the Respondent to rebut this presumption of anticompetitive harm. *Marine Bancorporation, Inc.*, 418 U.S. 602, 631 (1974); *Heinz*, 246 F.3d at 715; *Baker Hughes*, 908 F.2d at 982-83. Courts have examined evidence of ease of entry, *Baker Hughes*, 908 F.2d at 987-89; *Cardinal Health*, 12 F. Supp. 2d at 54-58; *United Tote*, 768 F. Supp. at 1071-82; *see Heinz*, 246 F.3d at 715 n.7; and efficiencies, *Heinz*, 246 F.3d at 720-22; *Staples*, 970 F. Supp. at 1086-88; among other issues, in considering whether the presumption from concentration has been rebutted. As the D.C. Circuit has twice held, "the more compelling the *prima facie* case, the more evidence the defendant must present to rebut it successfully." *Heinz*, 246 F.3d at 725 (quoting *Baker Hughes*, 908 F.2d at 991).

43. The presumption that flows from showing that the acquisition would significantly increase concentration cannot be overcome merely by arguing that the market would remain competitive. Once Complaint Counsel have made out a prima facie case of market concentration, "the burden [is] then upon [Respondent] to show that the concentration ratios . . . did not accurately depict the economic characteristics of the . . . market." *Marine Bancorporation*, 418 U.S. at 631, 94 S. Ct. at 2875. "To meet their burden, the defendants must show that the market-share statistics . . . 'give an inaccurate prediction of the proposed acquisition's probable effect on competition.'" *Cardinal Health*, 12 F. Supp. 2d at 54, (quoting *Staples*, 970 F. Supp. at 1083; *see Baker Hughes*, 908 F.2d at 991.

44. "To meet their burden, the defendants must show that the market-share statistics . . . 'give an inaccurate prediction of the proposed acquisition's probable effect on competition.'" *Cardinal Health,* 12 F. Supp. 2d at 54 (quoting *Staples*, 970 F. Supp. at 1083). The showing Respondent must make to rebut the presumption that flows from a substantial increase in concentration is an evidentiary showing; Respondent cannot rebut the presumption with mere argument. The court's decision in *Cardinal Health* makes that point clear: The court carefully considered defendants' evidence on entry, among other defenses, determined that the evidence was insufficient to demonstrate that entry would be sufficient to restore competition, and concluded that "the record developed at trial is not strong enough for the Court to conclude that the Defendants' claim of entry and expansion is sufficient to rebut the Government's prima facie case." 12 F. Supp. 2d at 58. Likewise, even where "buyer power exists in the whole market . . . , it alone cannot rebut the Government's prima facie case." *Id.* at 61. Thus, as *Cardinal Health* clearly holds, merely coming forward with any evidence is insufficient to rebut the prima facie case made from a showing of market concentration; Respondent must come forward with

sufficient evidence, in light of all the evidence, to support its defenses. *Accord Ivaco*, 704 F. Supp. at 1423-29 (reviewing and rejecting defendants' arguments that the market would continue to be competitive).

45. Respondent will be unable to produce significant evidence rebutting the presumption of violation. *Baker Hughes*, 908 F.2d at 988; *Cardinal Health*, 12 F. Supp. 2d at 54; *Staples*, 970 F. Supp. at 1083. The D.C. Circuit has recognized that the presumption is not automatically rebutted by the presentation of *any* evidence by the defendant, however scant. *Baker Hughes*, 908 F.2d at 988 ("if the totality of a defendant's evidence suggests that entry will be slow and ineffective, then the district court is unlikely to find the prima facie case rebutted").[2]

46. The Commission need not determine that competition will in fact be diminished, *Heinz*, 246 F.3d at 719, but direct evidence of a loss of competition should negate any attempt to rebut Complaint Counsel's *prima facie* case. *See Toys 'R Us v. Federal Trade Comm'n*, 221 F.3d 928, 937 (7th Cir. 2000) (proof of market effects makes "elaborate market analysis" unnecessary).

47. Even if Respondent succeededs in rebutting the presumption of violation, Complaint Counsel has carried its ultimate burden of persuasion that the acquisition would significantly reduce competition.

A. The Speculative Prospect of Entry by New Competitors Is Insufficient To Eliminate the Anticompetitive Effects of the Acquisition

48. For entry to rebut the presumption of anticompetitive effect, the evidence must show not merely that a firm might enter, but that "entry into the market would likely avert

---

[2] The D.C. Circuit recognized that the Supreme Court has described the presumption from concentration as heavy, and requiring a clear showing to rebut. *Id.* at 989-90. The D.C. Circuit nonetheless concluded that a "clear" showing is unnecessary, even while recognizing that the Supreme Court has not overruled its precedents. *Id.* at 990-91.

anticompetitive effects from [the] acquisition." *Staples*, 970 F. Supp. at 1086, (quoting *Baker Hughes*, 908 F.2d at 989; *accord Swedish Match*, 131 F. Supp. 2d at 170; *Cardinal Health*, 12 F. Supp. 2d at 55. Where entry is "difficult and improbable," that fact "largely eliminates the possibility that the reduced competition caused by the merger will be ameliorated by new competition from outsiders and further strengthens the FTC's case." *Heinz*, 246 F.3d at 717.

49. Entry must be "timely, likely, and sufficient in its magnitude, character and scope to deter or counteract the competitive effects" of a proposed transaction. *Merger Guidelines* § 3.0; *see Cardinal Health*, 12 F. Supp. 2d at 55-58 (adopting "timely, likely, and sufficient" test). In order for entry to be sufficient to restore competition, it must be entry that replaces the competition that existed prior to the acquisition. *Cardinal Health*, 12 F. Supp 2d at 58; *see also United Tote*, 768 F. Supp. at 1082 (rejecting entry defense when "entry . . . would not constrain anticompetitive price increases by incumbents"). "[T]he Court must consider whether, in this case, 'entry into the market would likely avert anticompetitive effects from [Staples'] acquisition of [Office Depot].'" *Staples*, 970 F. Supp. at 1086 (quoting *Baker Hughes*, 908 F.2d at 989). Similarly, in *Cardinal Health*, the court found that defendants had failed to come forward with sufficient evidence of sufficiency of entry (and of likelihood of entry) to rebut the presumption from concentration. 12 F. Supp. 2d at 58. If entry could be profitable at premerger prices without exceeding the likely sales opportunities--opportunities that include pre-existing pertinent factors as well as the merger-induced output reduction--then such entry is likely in response to the merger. *Merger Guidelines* § 3.0, 3.3.

50. In both *Baker Hughes* and *United Tote*, the court focused on the volatility of market shares to assess the prospect that an entrant could grow sufficiently to defeat an anticompetitive price increase. Even a showing of *actual* entry (absent here) is insufficient to

alleviate concern, unless that entry also indicates the likelihood of sufficient growth:

> The crucial aspect of *Baker Hughes* was not that actual competitors had entered the market and established a toehold but rather that the leading firm's "growth suggests that competitors not only can, but probably will, enter or expand if this acquisition leads to higher prices.

United Tote, 768 F. Supp. at 1081 (citations omitted). Thus, "evidence of frequent entry, but on a small scale without significant expansion by fringe firms, may also suggest the existence of barriers to entry on a large scale." Id. There is *no* evidence of frequent and profitable entry and *growth* in this industry that would suggest that these anticompetitive mergers would be alleviated by any such entry and growth.

51. In both *Baker Hughes* and *United Tote*, the courts also examined changes in market share over time -- particularly that of fringe players. *Compare Baker Hughes*, 908 F.2d at 989 (noting that Secoma had become the market leader within four years of making its first sale) *with United Tote*, 768 F. Supp. at 1081 & n.15 (fringe firm had only made two sales in 3-4 years). Here, there has been no entry during the two-to-three-year period since the acquisitions. AI Nastran -- Respondent's best evidence of entry -- has yet to make a single sale. This is a far cry from the growth that impressed the *Baker Hughes* court -- from no sales to industry leader in the same time frame. 908 F.2d at 989.

52. There are substantial barriers to entry into Nastran, as confirmed by Respondent's own documents..

B. Buyer Power Will Not Prevent the Exercise of Post-Acquisition Market Power By MSC

53. Buyer power will not counteract the exercise of market power by MSC. The "power buyer" defense has been given little weight. *University Health,* 938 F.2d at 1213 n.13 (granting preliminary injunction "given the FTC's strong showing that the proposed acquisition is

likely to lessen competition substantially . . . we think that the existence of these sophisticated purchasers in the relevant market, which may inhibit collusion, is insufficient to overcome the FTC's case"); *see also Cardinal Health,* 12 F. Supp. 2d at 61 (buyer power "alone cannot rebut the government's prima facie case."); *United Tote,* 768 F. Supp. at 1085 (buyers consisted of a handful of sophisticated buyers and "at least one hundred nine facilities unprotected"); *Alliant Techsystems,* 808 F. Supp. 9 (granting preliminary injunction even though there was only one buyer -- the United States military -- in the market and that buyer was not opposed to the merger).

54. The courts in *Cardinal Health, University Health, United Tote,* and *Alliant* granted the government's preliminary injunction motion even though defendants alleged the presence of "power buyers," which varied from 1 to 255 in number, accounted for up to $5 billion in purchases, and represented up to 90% of the market.

55. Because even MSC's largest customers have little leverage against MSC, "power buyers" will not counteract the likely anticompetitive effect of the acquisitions.

VIII. THE ACQUISITIONS ARE LIKELY TO RESULT IN A SIGNIFICANT LESSENING OF COMPETITION IN A RELEVANT ANTITRUST MARKET

56. But for these acquisitions, the competitive constraints imposed by UAI and CSAR on MSC were likely to remain the same or grow.

57. In a market with few players and no significant likelihood of entry, a merger that eliminates one of a small number of players is a matter of great concern. In *Coca-Cola*, a court blocked Coca-Cola's proposed merger of Dr Pepper, which had only a 4.6% market share, because "if the proposed acquisition is consummated there will be one less independent factor in the market to challenge the dominance of Coca-Cola Company." 641 F. Supp. at 1138. Here,

the two acquired companies, though small, were customers' only realistic alternative to MSC.

58. The acquisitions eliminated aggressive competitors in a highly concentrated market, which increases the risk that prices will rise after the acquisition. *Federal Trade Comm'n v. Food Town Stores, Inc.*, 539 F.2d 1339, 1345 (4th Cir. 1976) (enjoining merger when merging firms have been "aggressive competitors in the past," opening up stores in each other's markets and increasing sales by greater than the industry sales average).

59. In addition, even if the market is broader than advanced Nastran, MSC's unilateral market power is still enhanced, and the remaining firms would be able to coordinate pricing and bidding after the acquisition, in a manner that will reduce competition. Courts recognize 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. "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." *PPG*, 798 F.2d at 1503; *see also Cardinal Health*, 12 F. Supp. 2d at 45 n.8. As the Supreme Court has observed, as concentration increases, "greater is the likelihood that parallel policies of mutual advantage not competition will emerge." *Alcoa*, 377 U.S. at 280, 84 S. Ct. at 1289.

60. Tacit coordination is particularly a concern where entry barriers are significant, as in this case. Where entry into a market is slow, "colluding sellers need not fear that any attempt to restrict output in order to drive up price will be promptly nullified by new production." *Elders Grain*, 868 F.2d at 905; *Warner Communications*, 742 F.2d at 1162-63; *United States Steel Corp. v. Federal Trade Comm'n*, 426 F.2d 592, 604 (6th Cir. 1970). High entry barriers protect "the market power of existing firms and intensif[y] their ability to wield oligopolistic and

anticompetitive practices with relative impunity." *Id.*; *see also Fruehauf Corp. v. Federal Trade Comm'n*, 603 F.2d 345, 357 (2d Cir. 1979) (high entry barriers may be a signal that a particular merger carries a potential for impairing competition).

61. Courts have found violations based on concerns over coordination where the decrease in the number of competitors was less significant than in this case. *See Elders Grain*, 868 F.2d at 902 (reduction from 6 to 5 competitors); *Hospital Corp. of America*, 807 F.2d at 1387 (reduction from 11 to 7 competitors); *Bass Bros.*, 1984-1 Trade Cas. ¶ 66,041, at 68,609-10 (reduction from 7 to 5).

62. Complaint Counsel need not show a likelihood of explicit collusion. Section 7 seeks to prevent market structure that enhances the ability to engage in both explicit and tacit collusion. "The relative lack of competitors eases coordination of actions, explicitly *or implicitly*, among the remaining few to approximate the performance of a monopolist." *PPG*, 628 F. Supp. at 885 n.9 (emphasis added); *see also Brooke Group*, 509 U.S. at 229-30, 113 S. Ct. at 2591 ("In the § 7 context, it has long been settled that excessive concentration, and the oligopolistic price coordination it portends, may be the injury to competition the Act prohibits"); *Hospital Corp.*, 807 F.2d at 1386; 4 Areeda ¶ 916, at 85 (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.").

63. Coordination need not be perfect to cause anticompetitive harm. Section 2.11 of the *Merger Guidelines* observes that

> Terms of coordination need not perfectly achieve the monopoly outcome in order to be harmful to consumers. Instead, the terms of coordination may be imperfect and incomplete -- inasmuch as they omit some participants, omit some dimensions of competition, omit some customers, yield elevated prices short of monopoly levels, or lapse into episodic price wars -- and still result in significant

competitive harm.

X RESPONDENT WILL NOT SUSTAIN ITS BURDEN OF REBUTTING THE OVERWHELMING PRIMA FACIE SHOWING OF LIKELY ANTICOMPETITIVE EFFECTS FROM THE ACQUISITIONS

64. The *Merger Guidelines* require that, to be cognizable, any efficiencies must merger-specific, verifiable, and likely to prevent price increases in the relevant market. *Merger Guidelines* § 4.

65. An efficiency is merger specific only if it is "unlikely to be accomplished in the absence of either the proposed merger or another means having comparable anticompetitive effects." *Merger Guidelines* § 4; *see Heinz*, 246 F.3d at 721 ("[T]he asserted efficiencies must be 'merger-specific' to be cognizable as a defense. That is, they must be efficiencies that cannot be achieved by either company alone because, if they can the merger's asserted benefits can be achieved without the concomitant loss of a competitor."); *see also Federal Trade Comm'n v. University Health, Inc.*, 938 F.2d 1206, 1222 n.30 (11th Cir. 1991) ("[I]t might be proper to require proof that the efficiencies to be gained cannot be secured by means that inflict less damage to competition, such as internal expansion of merger with smaller firms.").

66. The efficiency must also be verifiable; that is, the proponent must "substantiate efficiency claims so that the [Commission] can verify by reasonable means the likelihood and magnitude of each asserted efficiency." *Merger Guidelines* § 4.

67. The proffered efficiencies must likely "be sufficient to reverse the merger's potential to harm consumers in the relevant market, *e.g.*, by preventing price increases in that market." *Id.*; *see Cardinal Health, Inc.*, 12 F. Supp. 2d at 63 ("The critical question raised by the efficiencies defense is whether the projected savings from the mergers are enough to overcome the evidence that tends to show that possibly greater benefits can be achieved by the public

through existing, continued competition.").

68. Efficiencies are not cognizable where they would not "be sufficient to reverse the merger's potential to harm consumers in the relevant market, e.g., by preventing price increases in that market." *Merger Guidelines* § 4. Accordingly, efficiencies that reduce only fixed costs are disregarded because they do not lower the variable costs of production, and therefore are unlikely to benefit consumers. In contrast, efficiencies that reduce the variable cost of production are far more likely to be passed along to consumers. *Cf. Heinz*, 246 F.3d at 721 (discussing proffered reductions in variable manufacturing costs).

69. Sizable efficiencies are necessary to justify a three-to-one merger. *See Merger Guidelines* § 4 ("The greater the potential adverse competitive effect of a merger . . . the greater must be cognizable efficiencies in order for the agency to conclude that the merger will not have an anticompetitive effect."). "[T]he high market concentration levels present in this case require, in rebuttal, proof of extraordinary efficiencies," *Heinz*, 246 F.3d at 720, and those efficiency claims must be tested in "a rigorous analysis . . . in order to ensure that those 'efficiencies' represent more than mere speculation and promises about post-merger behavior." *Id.* at 721. Respondent thus faces a heavy burden in attempting to demonstrate their asserted efficiencies. *See University Health*, 938 F.2d at 1223 ("defendant [cannot] overcome a presumption of illegality based solely on speculative, self-serving assertions"). Furthermore, before crediting any efficiencies, MSC must demonstrate and the Commission must find "that these economics ultimately would benefit competition and, hence, consumers." *Heinz*, 246 F.3d at 720 (quoting *University Health*, 938 F.2d at 1223). Accord, *Staples*, 970 F. Supp. at 1090 (finding that defendants had failed to prove the portion of their cost savings that would be passed on to customers as lower prices).

70. Furthermore, there is no assurance that the efficiencies, whatever they may be, will ever benefit consumers. As courts have recognized, competition is the force that drives efficiency and that allows consumers to receive the benefits that the market can produce: "[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; *see also United States v. Western Elec. Co.*, 592 F. Supp. 846, 874 (D.D.C. 1984) (competition results in "lower prices, highest quality, and the greatest material progress"), *appeal dismissed*, 777 F.2d 23 (D.C. Cir. 1985). As a result of the acquisitions, the competitive constraints imposed by UAI and CSAR no longer exist. As a result, the prices at which Respondent is able to maximize profits may in fact be considerably higher than its current prices, and its volume levels may be correspondingly lower.

71. MSC's purported efficiencies are insufficient to outweigh the likely anticompetitive effects of the acquisitions of UAI and CSAR.

IX. THE FAILING FIRM DEFENSE IS NOT AVAILABLE HERE

72. The failing-firm defense is available only where: "1) the allegedly failing firm would be unable to meet its financial obligations in the near future; 2) it would not be able to reorganize successfully under Chapter 11 of the Bankruptcy Act; 3) it has made unsuccessful good-faith efforts to elicit reasonable alternative offers of acquisition of the assets of the failing firm that would both keep its tangible and intangible assets in the relevant market and pose a less severe danger to competition than does the proposed merger; and 4) absent the acquisition, the assets of the failing firm would exit the relevant market." *Merger Guidelines* § 5.1; *see Dr. Pepper/Seven-Up Cos. v. Federal Trade Comm'n*, 991 F.2d 859, 864-65 (D.C. Cir. 1993) (setting

out test for failing-firm test).

73. MSC cannot meet its burden on a failing firm defense with respect to the acquisition of either CSAR or UAI.

X. MSC HAS ENGAGED IN UNFAIR METHODS OF COMPETITION THROUGH MONOPOLIZING AND ATTEMPTING TO MONOPOLIZE A RELEVANT ANTITRUST MARKET

74. The Sherman Act provides that it is unlawful to "monopolize, or attempt to monopolize . . . any part of the trade or commerce among the several States." 15 U.S.C. § 2. The Commission can prosecute violations of the Sherman Act as "unfair methods of competition" that are proscribed by section 5 of the Federal Trade Commission Act. *See, e.g., Federal Trade Comm'n v. Motion Picture Advertising Serv. Co.*, 344 U.S. 392, 394 (1953).

75. The offense of monopolization consists of "(1) the possession of monopoly power in a relevant market, and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident." *United States v. Grinnell Corp.*, 384 U.S. 563, 570-71 (1966).

76. The offense of monopolization is complete with the acquisition or maintenance of monopoly power; that power does not have to be exercised. *Berkey Photo v. Eastman Kodak Co.*, 603 F.2d 263, 275 (2d Cir. 1979) ("Unlawfully acquired power remains anathema even when kept dormant"), *cert. denied*, 444 U.S. 1093, 100 S.Ct. 1061 (1980). Proof of a change in price or output in the marketplace is not required so long as the conduct in question has resulted in the power to effect the market. *See Eastman Kodak Co. v. Image Technical Services, Inc.*, 504 U.S. 451, 464 (1992).

77. The essential elements of an attempt to monopolize are: (1) specific intent to control prices or destroy competition in some part of commerce; (2) predatory or anticompetitive

conduct directed to accomplishing the unlawful purpose; and (3) a dangerous probability of success. *Spectrum Sports, Inc. v. McQuillan*, 506 U.S. 447, 456 (1993).

78. The acquisitions of CSAR and UAI by MSC satisfies all the elements for monopolization and attempted monopolization.

X. SUBSTANTIAL RELIEF IS NECESSARY HERE

79. The purpose of the remedy is to restore competition. This does not limit the remedy to putting someone in the same position as the acquired firm at the time of the acquisition. Rather, "[t]he object of the [remedy] must be to place New Company in the same relative competitive position vis-a-vis [the defendant] . . . as that which [the acquired firm] enjoyed immediately prior to the illegal merger." *Utah Public Serv. Comm. v. El Paso Natural Gas Co.*, 395 U.S. 464, 470 (1969). A remedy that gives a new competitor the same assets that the acquired firm held at the time of the acquisition may be inadequate in light of post-closing events or changes. *Id.* Additional assets may be needed to put the new competitor "in the same *relative* competitive position" as the acquired firm. *Id.* (emphasis added).

80. The Commission has "wide discretion" in its choice of an antitrust remedy. *Atlantic Refining Co. v. Federal Trade Comm'n*, 381 U.S. 357, 376 (1965). For violations of section 7 of the Clayton Act, divestiture -- rather than conduct prohibitions such as a price ceiling -- is the favored remedy. "Divestiture has been called the most important of antitrust remedies. It is simple, relatively easy to administer, and sure. It should always be in the forefront of a court's mind when a violation of section 7 has been found." *United States v. E.I. du Pont De Nemours and Co.*, 366 U.S. 316, 329-31 (1961) (acquisition of 23% stock interest in another company deemed illegal under the Clayton Act is remedied by divestiture or sale of the stock rather than limiting voting rights).

81. "[I]t is well settled that once the Government has successfully borne the considerable burden of establishing a violation of law, all doubts as to the remedy are to be resolved in its favor." *du Pont*, 366 U.S. at 334. Complaint Counsel's divestiture remedy is favored over any conduct remedy offered by the Respondent. In *Cardinal Health*, the district court rejected defendant's offer of a price ceiling as a remedy for the challenged acquisitions. 12 F. Supp. 2d at 67. The defendant in *Cardinal Health* was "willing to allay any concerns of price gouging by representing that they would not raise the charge for their services." *Id.* The court rejected that approach, noting that such conduct remedies or price restrictions could in fact harm consumers. *Id.*

82. "Those who violate the [Clayton] Act may not reap the benefits of their violations and avoid an undoing of their unlawful project on the plea of hardship or inconvenience." *du Pont*, 366 U.S. at 326-27. Similarly, "the Government cannot be denied [an effective remedy] because economic hardship, however severe, may result." *Id.*; *see also El Paso Natural Gas Co.*, 395 U.S. at 471-72 ("We have emphasized that the pinch on private interests is not relevant to fashioning an antitrust decree, as the public interest is our sole concern"). In light of this principle of antitrust remedies, the Supreme Court in *du Pont* found that it was reversible error for the district court to be swayed by the fact that a divestiture would result in the defendant paying about $200 million in capital gains taxes. *du Pont*, 366 U.S. at 326-27; *see also El Paso Natural Gas*, 395 U.S. at 471-72 (financial impact of remedy on defendant not given any weight).

83. The Supreme Court evaluated a post-closing merger remedy in the natural gas industry. *Cascade Natural Gas Corp. v. El Paso Natural Gas Co.*, 386 U.S. 129 (1967). It reversed a district court's decree in which the defendant was "saving the cream for itself and

foisting the 'cats and dogs' on the New Company" which would receive the divested assets. *Id.* at 136-37. Post-closing the defendant had taken financial assets from the acquired firm and sought a divestiture allowing it to retain those assets. *Id.* The Supreme Court determined that such an approach was improper, as the "plan of divestiture . . . must establish a New Company in the same or comparable competitive position that [the acquired firm] was in when the illegal merger obliterated it." *Id.* at 139. The New Company "must be a viable, healthy unit, as able to compete as [the acquired firm] was when it was acquired." *Id.*

84. Firms like MSC cannot obtain competitive advantages by cherry-picking the assets acquired through an acquisition that violates the antitrust laws. The Commission dealt with post-closing commingling of assets in *Crown Zellerbach Corp.*, 54 F.T.C. 769 (1957). The Commission's order in *Crown Zellerbach* required the divestiture of an acquired plant that had been modernized post-acquisition. The respondent argued that divestiture of the plant would be an unreasonable remedy given that it had made about $15 million worth of improvements post-closing. *Id.* at 806-07. In rejecting the argument, the Commission stated that "the broad purpose of the statute cannot be thwarted merely because respondent has commingled its own assets with those of the acquired firm."

85. The Commission should not attempt to remedy these acquisitions by having MSC divest outdated assets. In *Automatic Data Processing* ("*ADP*"), the FTC faced a situation in which assets became outdated post-closing. 124 F.T.C. 456. ADP and the acquired firm had been rivals in the supply of computer software and database services for automotive salvage yards. Post-closing, the acquired firm's system used to maintain data on automotive parts and assemblies had become outdated. *Id.*; *see also* David A. Balto & James M. Mongoven, *Antitrust Remedies in High Technology Industries*, Antitrust Report, at 34 ("There was a problem with

simple divestiture, however, because ADP had switched all AutoInfo customers to use the ADP interchange after the acquisition and failed to update the AutoInfo interchange, which quickly became obsolete."). Given the decline in the competitive significance of the acquired firm's product, the Commission in *ADP* found that competition could not be restored simply by divesting the acquired firm's former product. *Id.* Instead, the Commission ordered ADP to provide a paid-up, nonexclusive, royalty-free license to its own interchange. *Id.*

86. The Commission also dealt with obsolescence in *Diamond Alkali*, a challenged to a consummated merger in the cement industry. *In re Diamond Alkali*, 72 F.T.C. 700 (1963). Diamond Alkali had manufactured the relevant cement product at two plants. *Id.* It purchased the plant of its only rival. *Id.* After the acquisition, Diamond Alkali closed down and dismantled its two original plants and supplied customers solely from the acquired plant. *Id.* In fashioning the remedy, the Commission found that the sole remaining plant could not be segregated or divided. It stated that "[a]lthough it would be most desirable to have two competitors in the place of one now operating, it does not appear feasible at the present time," as the remaining plant "appears to be a unitary operation which does not admit of dismemberment." *Id.* Diamond Alkali argued that, as a consequence, there should not be any divestiture or remedy. The Commission rejected that argument and instead ordered Diamond Alkali to divest its cement manufacturing plant. *Id.* The Commission's reasoning was that Diamond Alkali, without the plant, would remain "a credible potential competitor" to the buyer of the divested plant. *Id.* This situation -- a single supplier and a strong potential entrant -- was deemed a better alternative than to allow Diamond Alkali to maintain its monopoly achieved through acquisition.

87. In both *Diamond Alkali* and *ADP*, the Commission faced the question of how to fashion a remedy when key assets have become outdated. In each case, the Commission

accounted for the post-closing obsolescence of assets (rather than view them as they existed at the time of closing) in remedying the loss of competition. Here, the Commission should require licensing of the MSC Nastran code, and not merely a divestiture of the outdated CSAR or UAI codes.

88. The Supreme Court in *El Paso Natural Gas* considered the treatment of post-closing developments or improvements. Post-closing the defendant had developed new gas reserves that would affect the competitive relation or balance between the defendant and any purchaser of the acquired firm's assets. The Supreme Court held that "the new gas reserves developed since the merger must be equitably divided between El Paso and the New Company." 395 U.S. at 136-37. Likewise, the Commission has ordered divestiture of improvements or developments in post-closing merger cases. For example, in *Monier Lifetile,* the Commission ordered a divestiture including "all improvements to existing products and new products developed" by the merged company through the time of divestiture. *In the Matter of Monier Lifetile LLC*, FTC Docket No. 9290.

89. The remedy order in this case should allow MSC's customer to cancel long term, paid-up contracts without liability. Otherwise, a newcomer will be unable to vie for business. The Commission has broad discretion to order termination or modification of contracts in fashioning relief. In *Federal Trade Comm'n v. L.G. Balghur Co.*, the Seventh Circuit upheld a Commission order requiring the defendant to terminate certain contracts as part of the remedy. 442 F.2d 1 (7th Cir. 1971). In a recent post-closing merger case brought by the Commission, the U.S. District Court for the District of Columbia issued an order allowing for termination of the defendant's contracts with customers. The order stated that "Defendant shall notify by first class mail any Customer who has any contract with Defendant . . . that the Customer may terminate

such contract or currently existing amendments thereto without any charge, penalty or cost, upon thirty (30) days notice, any time over a period of twelve months starting on the date that the notification is received by the Customer." *Federal Trade Comm'n v. The Hearst Trust*, Civ. No. 1:01CV00734 (D.D.C. 2001). This contract provision was designed to enable the purchaser of the divested assets to compete adequately.

90. Commission merger orders commonly include some additional relief to facilitate the new company's entry into the market. One common form of ancillary relief is the transfer of technical support or technical know-how to enable the new company to use the divested assets or technology. Another common form of ancillary relief is the transfer of key employees. *See, e.g.*, *Exxon Corp.*, FTC Dkt. No. C-3907 (2001); *Computer Sciences Corp.*, FTC Dkt. No. C-3991 (2001). The ancillary relief may vary depending on the preexisting assets of the new company. A company that already has knowledgeable personnel and experience in the relevant industry may have less need for the transfer of employees or for technical support. Thus, the particular ancillary relief should be tailored later upon the Commission's evaluation of any proposal for a new company to acquire the divested assets.

P. Abbott McCartney
Peggy D. Bayer
Michael G. Cowie
Kent E. Cox
Andrew J. Heimert
Karen A. Mills
Nancy Park
Patrick J. Roach
Counsel Supporting the Complaint
Bureau of Competition
Federal Trade Commission

Washington, D.C. 20580
(202) 326-2695
Facsimile (202) 326-3496

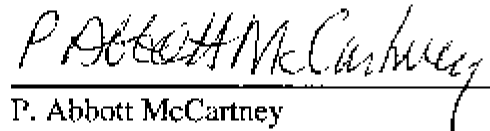
Dated: June 14, 2002

CERTIFICATE OF SERVICE

This is to certify that on June 14, 2002, I caused a copy of Complaint Counsel's Pre-Trial Proposed Conclusions of Law to be served on the following persons:

The Honorable D. Michael Chappell
Federal Trade Commission
600 Pennsylvania Avenue, N.W.
Washington, DC 20580

Tefft W. Smith, Esquire
Marimichael O. Skubel, Esquire
KIRKLAND & ELLIS
655 Fifteenth Street, N.W.
Washington, D.C. 20005
(202) 879-5034
Fax (202) 879-5200
Counsel for MSC.Software Corporation



P. Abbott McCartney

Dated: June 14, 2002