IN THE MATTER OF

THE PILLSBURY COMPANY, ET AL.

DISMISSAL ORDER, OPINION, ETC., IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT AND SEC. 7 OF THE CLAYTON ACT

Docket 9091. Complaint, Nov. 11, 1976 — Dismissal Order, June 15, 1979*

This order dismisses a complaint issued on November 11, 1976 charging a Minneapolis, Minn. manufacturer of food products with violating Section 7 of the Clayton Act and Section 5 of the Federal Trade Commission Act by acquiring Fox Deluxe Foods, Inc., a Chicago, Ill. producer and seller of frozen pizza. The Commission dismissed the complaint on ground that the merger is not illegal since it is unlikely to have significant anticompetitive effect in the national market for frozen prepared pizza.

Appearances

For the Commission: *Roger J. Leifer, Joseph Tasker, Jr.* and *Patricia S. Bangert.*

For the respondent: *John French* and *Randy L. Miller, Faegre & Benson* and *Dwight H. Oglesby,* The Pillsbury Company, all of Minneapolis, Minn.

COMPLAINT

The Federal Trade Commission, having reason to believe that the above-named respondents have entered into an agreement which, if consummated, would result in a violation of Section 7 of the Clayton Act, as amended, (15 U.S.C. 18), and Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45), and that said agreement therefore constitutes a violation of Section 5(a)(1) of the Federal Trade Commission Act, as amended, (15 U.S.C. 45(a)(1), and the Federal Trade Commission having reason to believe that the above-named respondent The Pillsbury Company has acquired the above respondent Fox Deluxe Foods, Inc. in violation of Section 7 of the Clayton Act, as amended, (15 U.S.C. 18) and Section 5 of the Federal Trade Commission Act (15 U.S.C. 45) and having found that a proceeding with respect to said violations is in the public interest, issues its complaint stating its charges as follows:

* Reported as amended by order of the administrative law judge dated June 17, 1977.

Definitions

(1) The term "The Pillsbury Company" as used herein means the Pillsbury Company and any parent companies thereof, and all of its subisdiaries, divisions, affiliates and the predecessors of any of the foregoing.

(2) The term "Fox Deluxe Foods, Inc." as used herein means Fox Deluxe Foods, Inc. and any parent companies thereof, and all of its subsidiaries, divisions, affiliates and the predecessors of any of the foregoing.

(3) The term "Frozen Prepared Pizza" means pizza which is cooked, processed or manufactured and frozen for sale.

The Pillsbury Company

(4) Respondent The Pillsbury Company (hereinafter "Pillsbury") is a Delaware corporation with its principal office at the Pillsbury Building, 608 Second Ave. South, Minneapolis, Minnesota.

(5) Pillsbury is a leading manufacturer and marketer of a wide range of food products, including prepared baking mixes, refrigerated dough products, flour and frozen prepared pizza.

(6) In its fiscal year ending May 31, 1976, Pillsbury had revenues in excess of $1.5 billion and net income in excess of $41 million. Pillsbury is among the two hundred largest United States corporations.

(7) In November 1975, Pillsbury entered the frozen pizza business by acquiring Totino's Finer Foods, Inc., a leading manufacturer and seller of frozen prepared pizza, with sales in excess of $39 million in its fiscal year ending October 31, 1975, which Pillsbury now operates as its frozen foods division. For its fiscal year ending October 31, 1976, Pillsbury's frozen food division had frozen prepared pizza sales in excess of $48 million. Retail sales of Pillsbury's frozen prepared pizza under the Totino's brand amounted to approximately $66.2 million for the fifty-two week period ending August 27, 1976, which makes Pillsbury the third largest frozen prepared pizza manufacturer in the United States.

(8) At all times relevant herein, Pillsbury has engaged and i engaged in commerce as "commerce" is defined in Section 1 of th Clayton Act, as amended, and the agreement between Pillsbury ar Fox set forth in Paragraph (13a) is a method of competition commerce as "commerce" is defined in Section 4 of the Fede Trade Commission Act, as amended.

Fox Deluxe Foods, Inc.

(9) Respondent Fox Deluxe Foods, Inc. (hereinafter "Fox") is an Illinois corporation with offices at 222 South Riverside Plaza, Suite 442, Chicago, Illinois.

(10) Before the acquisition set forth in Paragraph (13b), Fox manufactured or processed, and sold, food products including poultry, butter, eggs and frozen prepared pizza.

(11) In its fiscal year ended February 29, 1976, Fox had net sales of approximately $12.2 million, and assets in excess of $3.1 million. In that year, Fox had sales of frozen prepared pizza in excess of $7.3 million. Retail sales of Fox's frozen prepared pizza amounted to approximately $8.1 million for the fifty-two week period ending August 27, 1976, which made Fox the tenth largest frozen prepared pizza manufacturer in the United States, prior to its acquisition by Pillsbury set forth in Paragraph (13b).

(12) At all times relevant herein, Fox has engaged and is engaged in commerce as "commerce" is defined in Section 1 of the Clayton Act, as amended, and the agreement between Fox and Pillsbury set forth in Paragraph (13a) is a method of competition in commerce as "commerce" is defined in Section 4 of the Federal Trade Commission Act, as amended.

The Acquisition Agreement

(13a) On or about October 6, 1976, Pillsbury and Fox agreed in principle to the acquisition by Pillsbury of assets of Fox used in the production and sale of frozen prepared pizza (the "pizza assets"). On or about November 3, 1976, Pillsbury and Fox entered into an agreement which provides, *inter alia,* for the sale of the pizza assets 'n exchange for approximately $3 million worth of Pillsbury common tock. The practical result of the agreement, if consummated, would e the end of Fox's existence as an independent business entity.

The Acquisition

(13b) On or about November 15, 1976 Pillsbury acquired the pizza ;ets of Fox for approximately $3 million worth of Pillsbury nmon stock.

TRADE AND COMMERCE

Relevant Line of Commerce

t) The manufacture and sale of frozen prepared pizza is a :ate, distinct and relevant line of commerce. Frozen prepared pizza is one of the largest and fastest growing of all retail food sales categories. Calendar 1975 national retail frozen prepared pizza sales were estimated at approximately $394 million and, by the end of the fifty-two week period ending August 27, 1976, were estimated to have increased to approximately $447.6 million.

(15) Totino's brand frozen prepared pizza manufactured and sold by Pillsbury's frozen foods division and frozen prepared pizza manufactured and sold by Fox were, at the time of the acquisition set forth in Paragraph (13b), and had been for some time, in direct and substantial competition.

Relevant Section of the Country

(16) The relevant section of the country is the United States taken as a whole and certain metropolitan marketing areas within the United States.

Market Concentration

(17) Pillsbury and Fox, at the time of agreement and acquisition referenced in Paragraphs (13a) and (13b), and at all times relevant herein were substantial and direct competitors in the manufacture and sale of frozen prepared pizza in the United States as a whole and in a number of major metropolitan marketing areas.

(18) The United States frozen prepared pizza market is highly concentrated with the combined market share of the four largest firms (including Pillsbury) estimated to be in excess of 61%, before Pillsbury's acquisition of Fox, and the combined share of the eight largest firms estimated to be in excess of 84%, before Pillsbury's acquisition of Fox. At the time of the agreement and acquisition referenced in Paragraphs (13a) and (13b) and at all times relevant herein Pillsbury had approximately 14% of the national market while Fox had approximately 2%.

(19) At the time of the agreement and acquisition referenced in Paragraphs (13a) and (13b) and at all times relevant herein Fox and Pillsbury were substantial and direct competitors in the following highly concentrated marketing areas:

a. In the St. Louis marketing area, the four largest firms accounted for more than 78% of all retail frozen prepared pizza sales. Pillsbury was the largest in St. Louis with a market share of 22.13%; Fox was ranked seventh with 4.39%.

b. In the Houston, Texas marketing area the four largest firms accounted for approximately 90% of all retail frozen prepared pizz sales. Pillsbury was the largest in Houston with a market share of 39.0%; Fox was ranked fifth with a market share of 4.57%.

c. In the Charlotte, North Carolina marketing area, the four largest firms accounted for about 75% of all retail frozen prepared pizza sales. Fox was the third largest in that market with a market share of 14.65%; Pillsbury was ranked sixth with a market share of 6.01%.

d. In the Dallas/Ft. Worth marketing area the four largest firms accounted for about 78% of all retail frozen prepared pizza sales. Pillsbury was the largest in that market with a market share of 26.48%; Fox was ranked sixth with a market share of 7.5%.

(20) Fox and Pillsbury at the time of the agreement and acquisition referenced in Paragraphs (13a) and (13b) and at all times relevant herein were also substantial and direct competitors in certain other metropolitan marketing areas.

(21) Concentration in the frozen prepared pizza market has steadily increased over time.

Effects of the Acquisition

(22) The effects of the acquisition set forth in Paragraph (13b) may be substantially to lessen competition or tend to create a monopoly in the relevant markets in violation of Section 7 of the Clayton Act, as amended, (15 U.S.C. 18), and the acquisition and the agreement antecedent to the acquisition set forth in Paragraph (13a) each constitute an unfair method of competition and an unfair act or practice within the meaning of Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45), in the following ways among others:

a. the elimination of actual competition between Pillsbury and Fox in the United States frozen prepared pizza market;

b. the elimination of actual competition between Pillsbury and Fox in several major metropolitan marketing areas;

c. increased concentration in the manufacture and sale of frozen pizza in each of the areas described in (a) and (b) above;

d. the encouragement of further acquisitions and mergers by and among the other leading firms in the frozen prepared pizza market.

Violations

(23) The acquisition by Pillsbury of Fox's pizza assets for the reasons set forth herein constitutes a violation of Section 7 of the Clayton Act, as amended, (15 U.S.C. 18), and Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45).

(24) By entering into the agreement giving rise to the violation described in Paragraph (23), herein, Pillsbury and Fox have violated Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45).

Initial Decision by Joseph P. Dufresne, Administrative Law Judge

May 15, 1978

Background

In a complaint dated November 11, 1976, the Commission charged that respondents, The Pillsbury Company and Fox Deluxe Foods, Inc. (Pillsbury and Fox) would violate Section 7 of the Clayton Act, as amended, (15 U.S.C. 18), and Section 5(a)(1) of the Federal Trade Commission Act (FTCA) (15 U.S.C. 45) if they consummated an agreement they had made for Pillsbury to acquire Fox. It also was alleged that by entering into the agreement, Pillsbury and Fox had violated FTCA Section 5(a)(1). (Complaint, ¶¶ 1, 23 and 24.) [2]

Section 7, in pertinent part, reads as follows:

That no corporation engaged in commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital and no corporation subject to the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets of another corporation engaged also in commerce, where in any line of 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.

Section 5(a)(1) reads as follows:

Unfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce, are hereby declared unlawful.

On November 12, 1976, the day after the complaint originally issued, the United States District Court for the Northern District of Illinois, Eastern Division, in response to complaint counsel's request, issued a Temporary Restraining Order to prohibit consummation of the acquisition. Thereafter, on November 15, 1976, Fox and Pillsbury stipulated to a Preliminary Injunction (No. 76C-4190) which permitted the consummation of the acquisition upon certain conditions.

Pursuant to complaint counsel's motion, the complaint was amended on June 14, 1977, with the acquiescence of Pillsbury's counsel, to reflect that the challenged acquisition had taken place on or about November 15, 1976, and to thus seek divestiture of after-acquired property, relief which was not originally requested. (Amended complaint, ¶ 13B.)

The printed "First Amended Complaint" is dated June 22, 1977, and contains allegations that:

(a) The manufacture and sale of frozen prepared pizza is a separate, distinct and relevant line of commerce. Frozen prepared pizza is one of the largest and [3] fastest growing of all retail food sales categories. Calendar 1975 national retail frozen prepared pizza sales were estimated at about $394 million and by the end of the fifty-two week period ending August 27, 1976, were estimated to have increased to approximately $447.6 million. (¶ 14.)

(b) "Totino's" brand frozen prepared pizza manufactured and sold by Pillsbury's frozen foods division and frozen prepared pizza manufactured and sold by Fox were, at the time of the acquisition . . . and had been for some time, in direct and substantial competition. (¶ 15.)

(c) The relevant section of the country is the United States taken as a whole and certain metropolitan marketing areas within the United States. (¶ 16.)

(d) The United States frozen prepared pizza market is highly concentrated with the market share of the four largest firms (including Pillsbury) estimated to be in excess of 61%, before Pillsbury's acquisition of Fox and the combined share of the eight largest firms estimated to be in excess of 84%, before Pillsbury's acquisition of Fox. At the time of the agreement and acquisition . . . and at all times relevant . . . Pillsbury had approximately 14% of the national market while Fox had approximately 2%. (¶ 18.)

(e) The adverse effects of the acquisition alleged were:

1. The elimination of actual competition in the frozen prepared pizza market between Pillsbury and Fox in the United States as a whole and in several major metropolitan marketing areas (St. Louis, Mo.; Houston, Texas; Charlotte, N.C. and Dallas/Ft. Worth, Texas); [4]

2. Increased concentration in the manufacture and sale of frozen pizza in each of the areas described . . . above;

3. The encouragement of further acquisitions and mergers by and among the other leading firms in the frozen prepared pizza market. (¶ 22.)

Pillsbury's original Answer dated December 16, 1976, was changed and in lieu thereof, the Answer dated May 26, 1977, was substituted per my "Order Permitting Amendments to Answer," dated June 13, 1976. Fox's Answer was received by the Commission's Secretary on January 11, 1977; however, further consideration thereof is not warranted because complaint counsel advised on April 12, 1977, on the first day of the hearings, that the charges against Fox would not be pressed (Brickfield, Tr. 11–13).

In its Answer, Pillsbury made a general denial of each "allegation, matter, statement or thing" set forth in the complaint, except as otherwise expressly admitted or qualified in the Answer (Answer, ¶1). In addition, several affirmative defenses were asserted as follows:

(1) the complaint failed to state a claim upon which relief may be granted;

(2) the proceeding is not in the public interest;

(3) the acquisition of Fox by Pillsbury violated neither Clayton §7 nor FTCA §5 because Fox was a failing company at all times material to the acquisition;

(4) dismissal of the complaint with attorney's fees, costs and disbursements to Pillsbury, as provided by law, was requested. (Answer, pp. 4-5.)

A separate Answer to the Amended Complaint was not filed (French, Tr. 7). [5]

However, the first two affirmative defenses asserted by Pillsbury were negated by the Preliminary Injunction, entered into by all the parties. It provided that:

1. The complaint stated a claim upon which relief under Section 13(b) of the FTCA might be granted; and that an order would be in the public interest;

2. A new company would be formed by Pillsbury to carry on Fox's frozen prepared pizza business viably, separately and independently so that future divestiture would not be hindered if Pillsbury lost the case;

3. Commission representatives upon written request and reasonable notice could have access to any information relating to matters contained in the Court's Order and would be permitted to interview officers and employees of Pillsbury regarding any such matters;

4. The injunction is to continue in full force and effect until the complaint is dismissed by the Commission, set aside by a court on review or the Commission order has become final;

5. The parties agreed to expedite the administrative proceeding.

Pursuant to the Stipulation and Order, Pillsbury caused a new company, Fox Deluxe Pizza Company (Fox Pizza), to be established to carry on the frozen prepared pizza business of Fox. Pillsbury was also required to cause Fox Pizza to hire adequate personnel; to transfer $1,000,000 to Fox Pizza to be used to acquire manufacturing equipment and improve the Fox facilities; to cause at least 700,000 cases, or one-third of Fox Pizza's total annual production, to be Fox Pizza's own brand; to cause Fox Pizza to reinvest all earnings and pay no dividends; to cause Fox Pizza not to become insolvent; to enter into an Agreement whereby Fox Pizza manufactured pizza for Pillsbury; to use its best efforts to maintain the Fox Pizza brand in the marketplace and to improve the quality of the Fox Pizza product; [6] to refrain from using Fox Pizza's trade secrets or know-how; to notify all brokers selling the Fox Foods brand of pizza that Fox Pizza would continue to market and distribute product independently and in competition with Pillsbury; to refrain from interfering with the independent judgment of Fox Pizza or make any changes other than in the ordinary course of business; and not to permit any deterioration of Fox Pizza which might impair its capacity for the manufacture, distribution or sale of frozen prepared pizza. (Stipulation and Order, November 16, 1976; RPF 14.)

On November 24, 1976, the Commission instructed the administrative law judge to take all appropriate steps to expedite the proceedings and to submit brief, written quarterly reports to it as to the procedural status of the matter and the steps taken to effect expedition. ("Instructions to Administrative Law Judge" dated November 24, 1976.) The last of five such reports was submitted on February 14, 1978.

The case-in-chief was presented in Washington, D.C., on April 12–13, June 14, 20–23, 27–30, July 5–8, 11–14 and September 15, 1977. The case-in-defense was presented in Joplin, Missouri, on October 19–20, in Minneapolis, Minnesota, on October 25–28, and in Washington, D.C. on November 2, 3 and 8–11, 1977. Complaint counsel's case-in-rebuttal was presented in Washington, D.C. on December 7–8 and 13, 1977. Counsel for Pillsbury did not present a case-in-rebuttal after certain stipulations were worked out with complaint counsel, he had reviewed the complete transcript and had offered more evidence. Additional evidence, some offered by each side, was accepted per my Order dated February 13, 1978. The record was closed on February 14, 1978, per my Order dated January 23, 1978.

In total, 43 witnesses testified; 29 for the Commission and 14 for Pillsbury. There are 76 Commission exhibits and 72 Pillsbury exhibits. In accord with Commission Rule 3.43(g) those few exhibits which were rejected have been retained in the official record. There are 3818 pages of transcript of the adjudicative hearings. [7]

Bases for the Findings of Fact; Abbreviations Used

The findings of fact following are based on a review of the allegations made in the complaint, respondents' answers, the documentary evidence, and consideration of the demeanor of the witnesses. In addition, the proposed findings of fact, conclusions and proposed orders, together with reasons and briefs in support thereof filed by each side have been given careful consideration. To the extent not adopted by this decision in the form proposed or in substance, they are rejected.

For convenience, the findings of fact include references to supporting evidentiary items in the record. Such references are intended to serve as guides to the testimony, evidence, and exhibits supporting the findings of fact. They do not necessarily represent complete summaries of the evidence considered in arriving at such findings. The following abbreviations have been used:

Tr.	- Transcript, preceded by the name of the source of the information, followed by the page number.
CX	- Commission's Exhibit, followed by its number.
RX	- Respondents' Exhibit, followed by its number.
CCPF and CCB	- Complaint counsel's Proposed Findings and Brief
RPF and RB	- Respondents' Proposed Findings and Brief.

Findings of Fact

Commission Jurisdiction

1. Pillsbury is engaged in commerce as "commerce" is defined in Section 1 of the Clayton Act (Complaint and Answer, ¶ 8; RPF 5). Section 11 of the Clayton Act authorizes the Commission to enforce compliance with Section 7 of that Act (and other sections as well) with regard to acquisitions by corporations such as Pillsbury [8] (15 U.S.C. 21).

2. To and including November 15, 1976, Fox was engaged in commerce as defined in Section 1 of the Clayton Act. (Complaint and Answer, ¶12; RPF 9.) Being "in commerce," as defined in the Clayton Act also constitutes being "in commerce" under the FTC Act.

The Pillsbury Company

3. Pillsbury is a Delaware corporation with its principal office at the Pillsbury Building, 608 Second Ave. South, Minneapolis, Minnesota (Complaint and Answer, ¶4, RPF 1.)

4. Pillsbury is a manufacturer and marketer of a wide range of food products, including prepared baking mixes, refrigerated dough products, flour and frozen prepared pizza (Complaint and Answer, ¶5; RPF 2.) It also operates restaurant chains (*i.e.*, "Burger King," "Steak and Ale" and "Poppin Fresh Pie Shops") as subsidiaries. (Behnke, Tr. 19.)

5. In its fiscal year ending May 31, 1976, Pillsbury had revenues

in excess of $1.5 billion and net income in excess of $41 million. Pillsbury is among the 200 largest United States corporations. (Complaint and Answer, ¶6; RPF 3.)

6. Pillsbury acquired Totino's Finer Foods, Inc. (Totino's) in November 1975, a manufacturer and seller of frozen prepared pizza. Totino's gross sales for its fiscal year ended October 31, 1975, were approximately $39 million. For the twelve-month period ended October 31, 1976, Totino's gross sales as a Pillsbury subsidiary were approximately $48 million. (Complaint and Answer, ¶7; RPF 4.)

7. Pillsbury projects its profits from 1977 to 1981 to be a 10.6% return on invested capital, which is slightly lower than the average 11% return on investment for all manufacturing industries during the period 1960 to 1970. (Cady, Tr. 3340–41.) **[9]**

Fox Deluxe Foods, Inc.

8. Fox was an Illinois corporation with offices at 222 South Riverside Plaza, Suite 442, Chicago, Illinois. (Complaint and Answer ¶9; RPF 6.)

9. Immediately before its acquisition by Pillsbury on November 15, 1976, Fox was a manufacturer or processor and seller of food products including poultry, butter, eggs and frozen prepared pizza. (Complaint and Answer, ¶ 10; RPF 7.)

10. Fox had net sales of approximately $12.2 million and assets of approximately $3.1 million in its fiscal year ended February 29, 1976. Frozen pizza sales by Fox in that fiscal year were $7.3 million gross, $6.1 million net. (Complaint and Answer, ¶ 11; RPF 8.)

11. Fox was a "price brand" of frozen prepared pizza. The firm relied on the brand's relative low cost and frequent discount promotions, rather than high advertising activity, to attract business. (Francis, Tr. 660–61; DeLapa, Tr. 1206; CCPF 190.)

12. Prior to the acquisition, Fox's ability to obtain and keep geographic distribution varied. Its pizza was sold in a variety of areas in the Midwest and Southwest but did not remain in distribution in smaller areas within these larger ones for long periods. (Nickel, Tr. 493; RPF 112.)

13. As a part of the case-in-defense, there was a tour of the Fox plant in Joplin, Missouri on October 19, 1977 by the administrative law judge and counsel. Testimony was taken (Tr. 2144–2317). The witnesses were Donald E. Balster, Vice President of Operations of Fox Pizza (Balster, Tr. 2144), Rupert Spencer, Maintenance and Engineering Manager of Fox Pizza (Spencer, Tr. 2145), and John Jordan, Quality Assurance Manager of Fox Pizza (Jordan, Tr. 2218–

19). Areas observed and/or described during the tour are identified on floor plans entered in evidence as RX 12, RX 13, and RX 14.

14. Prior to the acquisition, 50 Fox production employees had been laid off. Since the acquisition, employment at the plant has grown from 75 to 180 production personnel and the plant has moved from one shift to two. (Balster, Tr. 2279-80; RPF 221.) [10]

15. The parties stipulated that had Dr. R.E. Baird, the U.S.D.A. circuit supervisor having jurisdiction over the Joplin plant testified, he would have said that before the acquisition: (a) the Fox plant was never completely rodent-proofed; (b) the meat room floor was deteriorating rapidly; (c) the cooker in the meat room leaked; (d) the oven in the bakery was difficult to clean and frequently caused fires among the pizza crusts; and (e) peeling paint on the walls of the sauce room and meat room necessitated daily scraping. Dr. Baird also would have said that at the time of the acquisition by Pillsbury, Fox had agreed with him to install a new ceiling in the bakery, correct deficiencies of the floor and walls in the meat room, and rodent-proof all exterior walls; however, it had not accomplished any of these corrections. (CX 76, ¶21; RPF 223.)

16. In mid-1975, there was a meeting between Mr. Joe Fox, chairman of the board of Fox, and Mr. William Bokman, a vice-president of Peavey Company. Mr. Bokman concluded that, although the company was for sale, it was not attractive to Peavey because: (a) Fox's frozen prepared pizza product was in the low-quality, low-price segment of the pizza business, in which Peavey had no interest; (b) there was very little or no management strength in the company; and (c) the new building, as described to him, did not sound like a major asset. (Bokman, Tr. 2597, 2599-2600; RPF 198.)

17. Previously, a Vice-President for Corporate Planning and Business Development of Anderson-Clayton Company, Houston, Texas, a food and food related producer/distributor had looked into the possibility of acquiring Fox. (Glasgow, Tr. 2854.) Mr. Glasgow met Mr. Fox and concluded that, although Fox was for sale, he perceived it as a relatively small company, with small sales, an old plant, a limited geographical area of operation, and a small regional brand at the low-price end of the market with nothing to recommend it to Anderson-Clayton. (Glasgow, Tr. 2858.) Mr. Fox did not recall discussions with anyone other than Peavey, Anderson-Clayton, and Pillsbury. (Fox, CX 46, p. 32; RPF 199.)

18. During the period 1972 to 1975, Fox earned substantial profits. Its sales increased from $6.4 million to $11.2 million; its total debt declined from $1.4 million to $860,000. The company reportedly had a current structure with working capital of $900,000 and current

ratio [11] of 2.15. Its net worth increased by over 50% to $1.7 million. However, in December of 1975, the company obtained a loan of $300,000 from Harris Trust and Savings Bank of Chicago, Illinois (Harris) to help finance its new plant at Joplin, Missouri. Harris was aware that the company was using short-term financing to finance long-term assets, but concluded that the proposed loan could be repaid in a year by means of liquidation of Fox's Hotel and Restaurant ("H&R") Division, which had become "a drag on profits" by generating "large losses." (RX 48; RX 49; RPF 179.)

19. In January of 1976, credit analysts at Harris expressed concern over losses by Fox in October and November 1975. (RX 51.)

20. Fox began pizza operations in Joplin on February 16, 1976. (CX 49, p. 1.) On March 22, 1976, production at Joplin was at 50–80% of capacity. On May 17, 1976, in a report to the directors of Fox, it was reported that: (a) sales for the first two months in Joplin were 20% below projections; (b) production efficiency was unfavorable; (c) severe competition, including competitive pricing below the Fox break-even point, was being encountered; and (d) losses at the H&R Division were draining off capital needed in the pizza business. (RX 16; RPF 186.)

21. On March 23, 1976, the Harris employee monitoring the loan, Barbara J. Pite, recommended a 90-day extension of the $300,000 loan. The sale of the H&R Division, which was to have enabled Fox Foods to repay the loan, had not taken place, and the H&R Division was continuing to incur losses. While the overseer of the loan thought that Fox's pizza operation had good earning potential, she told her supervisors that the frozen prepared pizza business "is very competitive and margins are narrow." Extension of the loan was approved, but with recognition of an uncertain operating outlook, the unprofitability of the H&R Division, and possible start-up problems in the company's new plant. (RX 52 and 53; RPF 180.)

22. On May 18, 1976, Ms. Pite recommended an additional $50,000 for Fox Foods from Harris. The operations in Joplin were not going as well as hoped with production costs running too high and margins being squeezed. (RX 54.) This $50,000 additional loan was approved but concern was expressed over Fox's failure to sell the H&R Division. (RX 55; RPF 181.) [12]

23. By May 19, 1976, "excessive downtime" appeared to require a further capital investment in equipment. At the same time more money was needed for co-op (supplier-reseller shared cost) advertising programs. (RX 17.) By June 8, 1976, intense competitive activity, with resulting price wars, appeared likely to force Fox to rely more

on private label as it became more difficult to compete with the major companies. (RX 20; RPF 187.)

24. By June 14, 1976, the chairman of Fox reported to the board of directors that no final offer had yet been received for the H&R Division. (CX 50.) The board also received a report from an outside consultant concerning the Joplin plant indicating that: (a) the economic advantages anticipated in moving to Joplin had not been realized; (b) much of the equipment transferred from Carthage to Joplin presented problems; (c) the baking environment was unsatisfactory and required several modifications; (d) the oven was unsuitable; (e) the topping line and processes were inefficient and wasteful; (f) the conveying system needed to be rearranged; and (g) the packaging machinery was not capable of meeting its goals. "As a minimum" the plant would require $61,820, and this would not include other needed changes, such as "rodent control curbs." (CX 50, pp. 3 & 4; RPF 188.)

25. On July 22, 1976, Ms. Pite asked that the Fox loan be raised by Harris to $500,000 and extended for another 90 days in the expectation that the H&R Division would be sold or liquidated or that all of Fox would be sold. (RX 56; RPF 182.)

26. By this time, Harris was considering a restructuring of the Fox debt that would have given Harris a security interest in Fox's receivables and inventory. (Weisenborn, Tr. 2811.) This would have resulted in an increase in the interest rate charged Fox Foods by Harris. (Weisenborn, Tr. 2843; RPF 183.)

27. By August 3, 1976, the negotiations for sale of the H&R Division had failed by reason of the refusal of the prospective purchaser to enforce collection of Fox's accounts receivable. (CX 51, p. 4.) By this time, Pillsbury had entered the scene with an offer to purchase Fox (CX 51, p. 5) but severe competitive pressures in the marketplace were hampering Fox's operations. Large food [13] corporations were bankrolling the pizza companies and intensifying competition in each market they entered. (RX 21.) The manager of the Joplin plant urged plant investment in excess of $258,000. (RX 15; RPF 189.)

28. That part of operations having to do with Fox's frozen prepared pizza business was profitable in its fiscal year ending February 23, 1976, (Boyce, Tr. 372) as well as during the period from March 1976 until the time of the acquisition in November 1976. (Boyce, Tr. 2395-96.) The Fox frozen prepared pizza business also was profitable in the months of September and October 1976 *(Id.)*; in the month of September alone, Fox showed a profit in the amount of $43,000. (CX 67; CPF 207.)

29. On November 15, 1976, the date on which Pillsbury acquired Fox, it was discovered by Pillsbury that $272,000 in signed but unmailed checks for debts owing to vendors were being held by Fox because of insufficient funds to cover them. (Walker, Tr. 2872–74, 2886; RX 59–63.) Pillsbury advanced $130,000 to cover the checks. (Walker, Tr. 2888.)

30. The causes of Fox's financial decline were: (a) its frozen pizza business was doing well but needed additional capital and (b) its H&R Division was incurring losses and encountering a variety of operating problems. (CX 47, p. 3.) Throughout fiscal 1975, freezer problems at the pizza plant in Carthage, Missouri, resulted in extraordinary expenditures averaging $30,000 per month above normal. (Boyce, Tr. 2408–09.) In addition, higher costs and prices and unusually warm autumn weather in late 1975 reduced pizza sales, with resulting losses in October and November of that year. (CX 48.) At the same time, the decision to transfer Fox's pizza operations to Joplin, Missouri, necessitated the financing at the Harris Trust, discussed above. Fox did have some prospect, in December of 1975, of selling its H&R Division, but only if it were willing to guarantee the accounts receivable. (CX 48, p. 2; RPF 185.)

31. Financial experts testified that:

(a) There was a very substantial deterioration in the company's financial position from 1975 through November of 1976 (Horsch, Tr. 2700);

(b) By November of 1976 the company's current assets-liabilities ratio had fallen to the point where not only [14] did it not have excess cash, but it was in need of substantial money (Horsch, Tr. 2700–01);

(c) Freezer problems at the old plant cost $30,000 per month and the move to the new plant was undertaken without effective long-term financing (Horsch, Tr. 2701);

(d) Start-up costs in Joplin had been underestimated by about $100,000 (*cf.* Boyce, Tr. 2414), and Fox never did inject sufficient capital into the new plant to enable it to produce in an efficient manner (Horsch, Tr. 2701);

(e) The company lacked the management to solve its problems; the chairman of the board was part-time and the president was really a sales manager; a full-time president was lacking. (Horsch, Tr. 2702; *cf.*, Weisenborn, Tr. 2822–23; CX 4, *in camera,* p. 12; Bokman, Tr. 2599–2600; Glasgow, Tr. 2858);

(f) A prompt infusion of new capital approximating $491,000 was urgently required by Fox in the autumn of 1976 (Horsch, Tr. 2705–09);

(g) It was extremely unlikely that such an infusion of capital would come from venture investment and to obtain it from a finance company would have resulted in much higher interest rates for Fox Foods (Horsch, Tr. 2714; Fitzgerald, Tr. 2972–84; RPF 192).

32. Complaint counsel's financial expert, Assistant Professor Peter Jones from the Harvard Business School (Jones, Tr. 3620) limited his testimony to the frozen prepared pizza operations of Fox. He said that the hotel and restaurant business clearly had to be closed or sold and that the future viability of Fox as a company depended on the future viability of the pizza business. (Jones, Tr. 3712.) He added that the H&R Division appeared to represent a drag which would not be acceptable, that his opinion as to Fox's viability turned on Fox's disposing of the H&R Division because "it was just a bad operation steadily for the past few years." (Jones, Tr. 3717–18, 3723–24; RPF 194–5.) **[15]**

33. In anticipation of consummation of the acquisition, Pillsbury caused the Fox cooked-meat room operations to be closed on November 1, 1976, and began to purchase cooked meat from Armour Foods. (RX 41; RPF 229.) After the acquisition, some Fox brand product was destroyed by Pillsbury and processed meat was purchased from another supplier until a new meat processing system could be installed. (Francis, Tr. 651–53; RPF 230.)

The Acquisition

34. On or about October 6, 1976, Pillsbury and Fox agreed that the former should acquire those assets of the latter which were used in the production and sale of frozen prepared pizza ("pizza assets") and on November 3, 1976, Pillsbury and Fox entered into an agreement whereby Pillsbury would acquire the "pizza assets" for $3 million in Pillsbury common stock. (Complaint and Answer, ¶ 13; RPF 10.) Pillsbury made the acquisition as agreed and immediately divested all assets of Fox not used in the manufacture and sale of frozen prepared pizza. (RPF 15.) However, pursuant to the Stipulation and Order issued by the district court, mentioned above, Fox was to be held separate as a corporate entity, *i.e.,* Fox Pizza, and to be operated by separate and independent management in Joplin, Missouri. (RPF 12–13.)

35. Pillsbury acquired Fox in an effort to satisfy short-term production requirements. (CX 2, *in camera,* p. 125; Levin, Tr. 149; Francis, Tr. 624.) Initially, Pillsbury intended to accomplish this

objective by entering into a contract-packing arrangement with Fox, but the food safety problems discovered at Fox eliminated the contract-packing alternative. (Levin, Tr. 224, 226–27; Francis, Tr. 625–26.)

Pizza Described

36. "Pizza" is a food having a bread dough base or crust that is almost always topped with a tomato-based sauce, cheese and may have garnishes such as pepperoni, sausage, mushrooms, anchovies, and the like. (Behnke, Tr. 25; Chamberlin, Tr. 1522; Francia, Tr. 1567; Kuphal, Tr. 2635–36; RPF 16.) [**16**]

37. Pizza is sold with a thick, thin, or a French bread crust. It may be square, oblong or round and may be sold whole or in slices. (RX 6, p. 2; Chamberlin, Tr. 1522–23; Barton, Tr. 1463–64; MacDonald, Tr. 2917; RPF 18.)

38. It may be sold to the consumer frozen, refrigerated, in a dry mix form, in ingredient form–that is, a consumer may purchase separately a grocery shelf-stable crust and make or purchase other ingredients for sauce and topping. (RX 25; RX 25A–25F; RX 27B–36B.) It also may be made from "scratch" at home, may be purchased freshly baked at a restaurant or pizzeria (a restaurant featuring pizza) or may be purchased unbaked or partially baked at a conventional restaurant or at a pizzeria. Pizza also is sold in bars and taverns, schools, grocery stores, military commissaries, delicatessens, vending machines, and other places where food is available for sale. (Behnke, Tr. 93; Caron, Tr. 998–99; Miller, Tr. 949; Follansby, Tr. 1618–19; Dursteen, Tr. 2323–24; Stauffer, Tr. 2107–08; MacDonald, Tr. 2924–25; RPF 19.)

39. Frozen prepared pizza has a shelf life of four to six months, as compared to the shelf life of refrigerated pizza which is five to eight days. (Behnke, Tr. 20–22; Perrin, Tr. 2511–12.)

40. Refrigerated pizza is displayed in the dairy case whereas frozen prepared pizza is displayed in freezer cabinets. (DeLapa, Tr. 1165–66.) There are chemicals which must be put into the dough, the cheese and the sauce to preserve a refrigerated pizza that need not be put into a frozen prepared pizza. (DeLapa, Tr. 1208–09; CCPF 98.)

41. Dry mix pizza has a longer shelf life than frozen prepared pizza. (Roxbury, Tr. 804) The sales trend of dry mix pizza is flat. The sales trend of frozen prepared pizza is up. (Roxbury, Tr. 795; Carpenter, Tr. 1349–50; CCPF 99.) [**17**]

Frozen Prepared Pizza-The Relevant Product Market

42. The manufacture and distribution of frozen prepared pizza in significant quantity is a development of relatively recent origin. For the most part, it is a business which had its beginnings in pizzeria restaurants started by families of predominantly Italian-American background. For example, Totino's, which is now owned by Pillsbury, began as a take-out pizzeria in 1952. In 1962 the Totinos decided to market frozen pizza at retail. (CX 10, p. 1.) Similarly, Saluto Foods, now owned by General Mills, began as a pizzeria in 1963. (DeLapa, Tr. 1073; CX 3, p. 3.) The "Tree Tavern" brand of pizza derives its name and origin (19 or 20 years ago) from the Tree Tavern restaurant in Paterson, New Jersey. (Francia, Tr. 1538-40.)

43. When they opened shop, frozen pizza manufacturers usually were small, local or regional businesses requiring little capital. This, because the manufacturing and distribution processes were relatively simple. (DeLapa, Tr. 1073-74; Francia, Tr. 1539-40; Pizza, Tr. 743-44.) Competition was not strong so these small companies were able to expand into many trade areas that would be difficult for them to enter today. (DeLapa, Tr. 1089; Pizza, Tr. 714; Caron, Tr. 1033; RPF 235.)

44. Frozen prepared pizza is produced by mixing dough and, by the pressed or sheeted method, reducing the thickness of the dough and cutting it into predetermined shapes of a specific size. If a sheeted method is employed, the crusts are "proofed," *i.e.,* placed in a piece of equipment where the temperature and humidity can be controlled for a long enough time to allow the product to rise. Crusts are then baked in an oven and transported on a conveyor belt to a topping area where sauce, cheese and other toppings are applied manually or automatically. The pizza is then frozen in a blast freezer (quick freezer) and packaged manually or automatically. (Behnke, Tr. 25-26; Francis, Tr. 609-12; Kuphal, Tr. 2645; CCPF 81.)

45. Most frozen prepared pizza contains no special ingredients differing from other forms of pizza. While each manufacturer may feel that his special blend imparts a special taste to his product, the ingredients of all forms of pizza are about the same. (DeLapa, Tr. 1074; Selby, Tr. 1247-50, 1258-59; RPF 46.) [18]

46. There is nothing in the manufacture and distribution of frozen prepared pizza which makes it an unusual food product. It is manufactured and then sold by food brokers who represent the manufacturers. Purchasers at this, the supply side of distribution, are wholesalers and chain grocery retailers. On the retailing side, wholesalers sell the product to resellers who, in competition with the

chain retailers, sell the pizza to the consuming public. (Patterson, Tr. 1739; RPF 80.)

47. Separate buying offices of the same retail food chain or the same voluntary wholesalers are viewed as separate and distinct customers. (Boyce, Tr. 366–67; Carlson, Tr. 560–61.) For example, among Fox's top ten customers are three different divisions of Winn-Dixie Stores, Inc., a retail food chain (CX 16); and among Totino's top ten customers are two different buying offices of Super-Valu Stores, a wholesaler, and two different buying offices of Safeway Stores, Inc., a retail food chain. (CX 26 *in camera;* CCPF 137.)

48. Food brokers typically represent a variety of manufacturers–"principals"–handling a large number of frozen and non-frozen food and non-food products in a single primary geographical area of responsibility. (Walling, Tr. 1321–22; Patterson, Tr. 1758–59; Carlson, Tr. 508–09; RPF 91.)

49. The boundaries of a broker's area of primary responsibility will vary according to the size of the broker organization and changing business conditions. (Walling, Tr. 1328–29; Patterson, Tr. 1754–55; Carlson, Tr. 570; Nickel, Tr. 451; Pizza, Tr. 738; Rosen, Tr. 1885; RX 1; Walling, Tr. 1312; Mosley, Tr. 1816–17; RPF 92.)

50. The process of preparing a frozen prepared pizza generally involves different methodologies and machinery than the process of making a pizzeria pizza. (DeLapa, Tr. 1074; Selby, Tr. 1232–36) Pizzeria pizzas generally are not frozen before sale to the customer and do not contain preservatives often found in frozen prepared pizzas. (Selby, Tr. 1235–36; CCPF 82.) **[19]**

51. Frozen prepared pizza can be manufactured on a large scale basis. When this is done, some of the machinery utilized may be customized. (Dursteen, Tr. 2331–32) Most of the machinery used in the manufacturing process is similar to machinery used to manufacture other baked goods or frozen foods. The equipment used to mix the dough, roll it out and bake it, is similar to equipment used in the mass manufacture of other baked goods. The conveying system within the factory appears to be standard. (*See* Finding 144 re plant tour). The blast freezer is typical of those used in the manufacture of any food which must be fast-frozen. (Kuphal, Tr. 2634–58; RX 58.)

52. Frozen prepared pizza can be manufactured in the kitchen of a restaurant and one witness began in a garage. (DeLapa, Tr. 1073; Francia, Tr. 1539–40) Frozen prepared pizza can be easily assembled by a few employees and frozen. (Stauffer, Tr. 2112–13.)

53. In the late 1960's, large conglomerate food companies began to enter the frozen prepared pizza market, usually by acquisition, changing the nature of competition within the frozen prepared pizza

industry. (Pizza, Tr. 714, 766; Malkowicz, Tr. 858; DeLapa, Tr. 1075, 1079–81; Francia, Tr. 1557; CCPF 25; CCPF 156.)

54. There is a trade association, the National Frozen Pizza Institute, to which many manufacturers of frozen prepared pizza belong. Pillsbury is a member. (Boyce, Tr. 383; Francis, Tr. 612; Pizza, Tr. 699; Malkowicz, Tr. 879; DeLapa, Tr. 1090.) The Institute is open primarily to domestic manufacturers of frozen prepared pizza but associate membership is available to others having an interest in the frozen pizza industry. (Pizza, Tr. 700; CCPF 26.)

55. Many manufacturers, whether they are independent firms or separate divisions of larger firms which produce frozen prepared pizza, do not produce other types of pizza. (CCPF 27 and 87.) For example:

a. Frozen Foods Division of Pillsbury (separate division producing only frozen pizza). (Francis, Tr. 608; Nickel, Tr. 402–03.) [20]

b. Fox (produces only frozen pizza). (Boyce, Tr. 341–42.)

c. Anthony J. Pizza Inc. (produces only frozen pizza). (Pizza, Tr. 679.)

d. Saluto Foods Corp. (separate division of General Mills producing only frozen pizza). (DeLapa, Tr. 1072.)

e. Ellio's Pizza (separate division of Purex producing only frozen pizza). (Malkowicz, Tr. 857, 885.)

f. Stouffer's Frozen Foods (produces only frozen pizza). (Stauffer, Tr. 2114.)

56. Plants producing frozen prepared pizza containing meat are U.S.D.A. inspected and subject to U.S.D.A. guidelines and regulations. (Francis, Tr. 627–28; DeLapa, Tr. 1148–51; Balster, Tr. 2202–03; CCPF 90.)

57. Frozen prepared pizza is a food product which must be kept frozen to avoid deterioration and must be stored and transported in a controlled temperature. (Caron, Tr. 1008–09; Perrin, Tr. 2534–36; CCPF 92.)

58. Manufacturers and brokers of frozen prepared pizza regularly "cut" (*i.e.,* have a taste test, usually for a reselling buyer) against competing brands of frozen prepared pizza. (Pizza, Tr. 701–02; Malkowicz, Tr. 883–84.) They rarely cut against any other products. (Pizza, Tr. 701–02; Malkowicz, Tr. 883–84; CCPF 29.)

59. Pillsbury "cuts" much more often against other brands of frozen prepared pizza than against dry mix, refrigerated or pizzeria pizza. (Behnke, Tr. 35–37; CCPF 30.)

60. Brokers of frozen prepared pizza cut against competing

brands of frozen prepared pizza but do not cut against dry mix, refrigerated or pizzeria pizza. (Moore, Tr. 1795-96; CCPF 31.)

61. Manufacturers of frozen prepared pizza regularly monitor the competitive activities of other manufacturers of frozen prepared pizza and do not regularly monitor the competitive activities of manufacturers of other products. (Boyce, Tr. 375-76; Pizza, Tr. 703-04; Carlson, Tr. 515-17, 530, 558-59; Malkowicz, Tr. 883; DeLapa, Tr. 1098-99; Carpenter, Tr. 1334-35; Barton, Tr. 1406-07; Chamberlin, Tr. 1480-81; Francia, Tr. 1548-49; Dursteen, Tr. 2332-33; CCPF 33-34.) [21]

62. Brokers do not report on the competitive activity of manufacturers of other products to manufacturers of frozen prepared pizza. (Carlson, Tr. 530; Walling, Tr. 1301; Patterson, Tr. 1748-49; Mosley, Tr. 1830-31; CCPF 35.)

63. Consumers view pizzeria pizza as a more desirable product than frozen prepared pizza. (Dursteen, Tr. 2346-47; Rowlatt-Smith, Tr. 3794-95; CCPF 76.)

64. They do not readily substitute other forms of pizza for frozen prepared pizza and are more likely to choose hamburgers, frankfurters or ingredients for salads as alternatives to frozen prepared pizza than refrigerated, dry mix or pizzeria pizza. (RX 64F; Neadle, Tr. 3125-26; Cady, Tr. 3407-08; CCPF 75.)

65. Manufacturers of frozen prepared pizza view pizzeria pizza as the "golden standard." (Nickel, Tr. 479-80; Chamberlin, Tr. 1516.) Generally they feel that frozen prepared pizza is of a lesser quality than pizzeria pizza. (DeLapa, Tr. 1106-07; Dursteen, Tr. 2346-48; Paulucci, Tr. 2424; CCPF 100.)

66. Most manufacturers of frozen prepared pizza view all food as competing for the consumer's food dollar, but see frozen prepared pizza as a distinct market and the primary source of their competition. (Pizza, Tr. 696-97; Roxbury, Tr. 842-43; DeLapa, Tr. 1098-99; Rowlatt-Smith, Tr. 3735-36; CCPF 44.)

67. Manufacturer-witnesses who listed specific competitors listed only other frozen prepared pizza manufacturers. (Pizza, Tr. 694-95; Roxbury, Tr. 821; Francia, Tr. 1550.) They did not look upon manufacturers of refrigerated pizza, dry mix pizza or pizzeria pizza as direct competitors. (DeLapa, Tr. 1098-99; Pizza, Tr. 695-96, 806; Carpenter, Tr. 1365-68; Francia, Tr. 1549; Barton, Tr. 1406; Stauffer, Tr. 2119; Paulucci, Tr. 2424; CCPF 46-49.)

68. In their pricing decisions, manufacturers of frozen prepared pizza consider the prices set by other manufacturers of frozen prepared pizza. (Boyce, Tr. 375-76; Francia, Tr. 643-44; Roxbury, Tr. 786-87; Malkowicz, Tr. 861; CCPF 192.) They do not take into account

the prices set by manufacturers of dry mix, refrigerated, pizzeria or institutional pizza in establishing their prices. (Roxbury, Tr. 794-95; Malkowicz, Tr. 861; Caron, Tr. 1008; CCPF 35, 37, 66-67, 104, 111.) [22]

69. Manufacturers of frozen prepared pizza regularly receive only data concerning frozen prepared pizza. (Francis, 621-22; CCPF 38.)

70. It is considered a conflict of interest for brokers to handle two manufacturers' frozen prepared pizzas at the same time. (Pizza, Tr. 704-05; DeLapa, Tr. 1117-18; Walling, Tr. 1290; Patterson, Tr. 1781-82.) The manufacturer of "John's" brand testified that he had lost brokers because of such conflicts. (Pizza, Tr. 707; CCPF 41.)

71. In its 1976 Annual Report, Pillsbury refers to "national retail frozen pizza sales." (CX 1, pp. 8-10; Francis, Tr. 616, 618; CCPF 61.)

72. Pillsbury views itself as competing against other manufacturers of frozen prepared pizza. Officials and documents of that company state that the major competitors of Totino's pizza are Celeste, Saluto, Jeno's, Tony's, Chef Boyardee and John's. (Francis, Tr. 639-40; CCPF 64.)

73. Brokers view other brands of frozen prepared pizza as the competition for the frozen prepared pizza which they handle. (Walling, Tr. 1277-79; Patterson, Tr. 1739-40; Mosley, Tr. 1817-19; CCPF 68.)

74. Retailers consider frozen prepared pizza as a separate product category, distinct from other product categories, such as frozen entrees or frozen orange juice. (Bahl, Tr. 289-90; Coles, Tr. 1587-89; Smith, Tr. 1639; Moore, Tr. 1797-99; Urbanowicz, Tr. 1854; CCPF 70.)

75. Frozen prepared pizza is evaluated in terms of movement or retail sales and profitability separately from any other category of product. (Bahl, Tr. 306; Coles, Tr. 1587-89; Smith, Tr. 1639-40; Moore, Tr. 1797-99; Urbanowicz, Tr. 1854; CCPF 71.) [23]

76. Case movement or rate of retail sales of frozen prepared pizza is not compared to case movement of dry mix or refrigerated pizza. (Coles, Tr. 1588-89; Moore, Tr. 1796-99; Urbanowicz, Tr. 1854; CCPF 72.)

77. Position and number of rows or "facings" (*i.e.,* the stack of any product in a retailer's freezer cabinet so that the top package faces the consumer) is of great importance to the sale of frozen prepared pizza. (Bahl, Tr. 293; Caron, Tr. 1003-05; DeLapa, Tr. 1110-12; Patterson, Tr. 1772-75.) Manufacturers of frozen prepared pizza compete against one another for position and number of facings in the frozen prepared pizza section of the freezer cabinet. (Caron, Tr. 1003-05; DeLapa, Tr. 1110-12; CCPF 94.)

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78. Heavy consumer oriented promotion and advertising are required to secure and retain adequate space in retailers' freezer cabinets. (Caron, Tr. 1003–04; DeLapa, Tr. 1084–85; Francia, Tr. 1558–59.) Frozen prepared pizza is in the top 10 to 12 percent of the frozen food products most heavily promoted. (Bahl, Tr. 295–96; CCPF 95.)

Statistical Reports Frozen Pizza Manufacturers Use

79. Manufacturers of frozen prepared pizza rely on reports published by Selling Areas Marketing, Inc., a subsidiary of Time, Inc. ("SAMI") for information on warehouse movement of frozen prepared pizza sold to food stores in defined areas of the United States. (Boyce, Tr. 361; Nickel, Tr. 405–11; Francis, Tr. 621–22; Pizza, Tr. 689; Malkowicz, Tr. 863; Miller, Tr. 951; DeLapa, Tr. 1115–16; Carpenter, Tr. 1333; Chamberlin, Tr. 1473–74; CX 54, p. 1; RPF 99.)

80. SAMI statistics are used for a wide variety of purposes. They are used "in evaluations of how the market quota is progressing" (Barton, Tr. 1395), "to mark the trends in the industry" (Nickel, Tr. 429; Francis, Tr. 621), "as a barometer of how well our broker is doing" (Nickel, Tr. 429); *see also* Chamberlin, Tr. 1474), "as a guide and cross reference to check our own information" (Moore, Tr. 1812), to mark "trends and directions," (MacDonald, Tr, 2951), and where deemed "useful for sales" (Chamberlin, Tr. 1477; RPF 135). [24]

81. Users rely on the SAMI data despite the fact that it is acknowledged not to include at least one of the largest frozen prepared pizza manufacturers (Schwan's) and possibly two (Tombstone) because they do not furnish SAMI with product movement data. (DeLapa, Tr. 1121; RPF 136.)

82. Mr. Chamberlin, Vice President, General Manager, frozen food operation of Quaker Oats (Celeste brand) testified that SAMI is the most practical and acceptable tool available to marketers to monitor market performance because it comes out quickly and can keep management relatively current. This, combined with the experience of management in the field, can provide a reasonably accurate picture of the marketplace. (Chamberlin, Tr. 1519–20; RPF 137.)

83. SAMI is a recognized market survey firm and reports on frozen prepared pizza as a distinct product category in various areas of the United States. (CX 54, p. 2; RX 11, Exhibit A, p. 2; CCPF 79.) When the acquisition occurred, 36 such areas were covered and in 1977, SAMI added three additional local areas to its system for a total of 39. (*See* RX 68.)

84. No witness from SAMI testified; however two stipulations

(CX 54 and RX 11), prepared in consultation with SAMI personnel, and which describe the preparation of SAMI reports, are in the record.

85. SAMI monitors (counts) warehouse withdrawals in areas estimated to encompass 75% of national grocery store sales (CX 54, ¶ 4; RX 11, ¶ 2) and, within those areas, it obtains warehouse withdrawal reports covering, on the average, about 80% of the included grocery products passing through grocery warehouses. (CX 54, ¶ 4; RX 11, ¶ 3; RPF 124.)

86. SAMI cannot statistically predict product movement patterns in other warehouses. (RX 11, ¶ 5.) Patterns of stocking and withdrawals may differ between warehouses which report to SAMI and warehouses which do not. (Kuehn, Tr. 3150; Douglas, Tr. 3455-3457; RPF 124.) [25]

87. SAMI is similarly unable to make a statistically verifiable prediction as to product movement in areas where it does not count movement. "SAMI does not know whether product movement patterns outside its reporting areas are the same as those inside those areas, or that patterns for unreported product movement within an area are the same as those for reported product movement in the same area." (Kuehn, Tr. 3151-56; RX 11, ¶ 14; RPF 124.)

88. Although SAMI counts the movement of private label products, it does not report such movement if there are less than three private label products within a reporting classification in a given reporting area. (RX 11, ¶ 4; RPF 124.)

89. SAMI relies in part on the reporting warehouses to filter out of their reports the products shipped outside defined reporting areas, but SAMI cannot assure that this is always done and SAMI does not insist on the filtering process if such outshipments amount to less than 10% of the total. (RX 11, ¶ 9; *see also* CX 54, ¶¶ 17-19; Kuehn, Tr. 3173, 3175-76; RPF 124.)

90. SAMI uses the same reporting areas to monitor the movement of numerous products (food and non-food, frozen and non-frozen), but this does not reflect any deliberative judgment by SAMI as to what the economic or geographic markets are for any product on which SAMI reports. No attempt has been made by SAMI to relate its reporting areas to food manufacturers' patterns of distribution. SAMI is not aware as to whether such patterns exist. Warehouses reporting to SAMI may ship to stores (a) within a single SAMI reporting area, or (b) within and outside such areas, or (c) into several such areas, or (d) a combination of "(b)" and "(c)" above. Some warehouses reporting to SAMI reportedly ship as much as 40% of their product outside SAMI reporting areas. Warehouses outside

SAMI marketing areas may also ship products into such areas. (RX 11, p. 5; RPF 100.)

91. SAMI developed fixed geographic boundaries for these local areas in order to provide reports that would be consistent over time. (CX 54, ¶ 14.) These boundaries were decided upon after SAMI personnel consulted with the local grocery trade in each area (CX 54, ¶ 12), often using in their consultation, markets defined by the trade publication "Progressive Grocer." (CX 54, ¶ 26; Nickel, Tr. 450-51.) [26]

92. SAMI also consulted with the trade in order to insure that the boundaries are not too narrowly drawn (CX 54, ¶¶ 14, 15); but not every local grocery distribution market is covered by the SAMI system (*see* CX 27, p. 10716; Caron, Tr. 1045; Carpenter, Tr. 1334, 1336). SAMI's local grocery distribution areas were designed to encompass the common business operations core of local grocery retailers as well as the wholesalers and the stores they supply. (CX 54, ¶ 14; CCPF 131.)

93. SAMI local marketing areas therefore serve as "rough approximations" of local grocery distribution markets. (Maps of the SAMI areas where Pillsbury's Totino's brand and Fox competed, are found as CX's 37-45.) SAMI areas are similar to broker territories. (Barton, Tr. 1395-96; CCPF 133.)

94. SAMI has developed its local market areas knowing that it would not be possible to cover all of the retail stores served by its participating food operators (the retail chain warehouse and wholesale grocery warehouse operators who submit their warehouse withdrawal data to SAMI). (CX 54, ¶ 3.) The resulting boundaries describe local grocery distribution areas that track warehouse distribution patterns as closely as possible using county lines as boundaries. (CX 54, ¶ 12; CCPF 130.)

95. Manufacturers of frozen prepared pizza rely on SAMI data to describe and analyze local grocery distribution/marketing conditions by brand name. (CX 17A, pp. 11110-11; CX 27 p. 10716; Boyce, Tr. 361-62; Nickel, Tr. 427-28, 432, 437, 439; Carlson, Tr. 510-11, 521-22, 530, Pizza, Tr. 689; Malkowicz, Tr. 864-65; DeLapa, Tr. 1185; Barton, Tr. 1394-96.)

96. Manufacturers often supply SAMI reports on frozen prepared pizza to brokers for use as selling tools to convince buyers for resellers that they should stock more of a particular brand. (Walling, Tr. 1293; Patterson, Tr. 1740; Rosen, Tr. 1882; CCPF 36.)

97. Pillsbury does not regularly subscribe for SAMI reports on products other than frozen prepared pizza except for one summary of

numerous grocery items. (Boyce, Tr. 363; Nickel, Tr. 429-30; Francis, Tr. 621-22; CCPF 37.) [27]

98. Two other market survey firms, Market Research Corporation of America ("MRCA") and A.C. Nielson, also report on sales of frozen prepared pizza as a distinct category of food product. (CX 69; Francis, Tr. 622; Roxbury, Tr. 803; CCPF 80.)

99. MRCA is a consumer diary panel data source. (Kuehn, Tr. 3246-47.) MRCA data are based on a random sample of consumers who fill out diaries each week indicating what products have been purchased by each member in a household. (*See, e.g.,* CX 69.) Such a diary includes product which is distributed by means of direct store delivery, as well as product which is distributed directly to the consumer. (Kuehn, Tr. 3191.) However, Dr. Kuehn testified that MRCA data also contained error. (Kuehn, Tr. 3242, 3260; RPF 141-42.)

100. According to CX 55 *(in camera)* ("SAMI Frozen Brand Shares of All Flavors — U.S. Total, Units: Dollars"), CX 60 *(in camera)* ("SAMI 20 Frozen Pizza Brand Shares of All Flavors — Total U.S., Units: Dollars") and CX 64 *(in camera)*("MRCA" Frozen Pizza Brand Shares of All Flavors — U.S. Total — 1974 through 1976, $(000's)"), the shares of frozen pizza sales in the United States held by various manufacturers were as follows:

CX 55

		1976	1975	1974
Jeno's	-	22.40%	21.65%	16.54%
Totino's	-	18.28%	17.07%	15.07%
Celeste	-	12.69%	12.65%	13.82%
John's	-	8.63%	8.83%	10.05%
Top Four	-	62%	60.20%	55.48%

CX 60

		1976	1975
Jeno's	-	18.82%	17.41%
Tony's	-	15.96%	19.58%
Totino's	-	15.36%	13.72%
Celeste	-	10.66%	10.17%
Top Four	-	60.80%	60.88%

[28] CX 64

		1976	1975	1974
Jeno's	-	15.7%	14.5%	11.0% (Totino's)
Totino's	-	13.7%	13.0%	10.7% (Jeno's)
Tony's	-	11.7%	13.0%	10.4%
Celeste	-	8.2%	7.0%	7.6% (Chef Boyardee)
Top Four	-	49.3%	47.5%	39.7%

Competition in the Frozen Prepared Pizza Industry

101. The evidence concerning (a) the size of the "frozen prepared pizza" market and (b) the shares of this line of commerce held by the major manufacturers is contained in CX 35 and 36. These were prepared by Schwan's Sales Enterprises, Inc., by combining information concerning Schwan's sales of "Tony's" pizza with data obtained from reports prepared by SAMI (Miller, Tr. 951-52); and CX 55-65, which were prepared by complaint counsel on the basis of data drawn from CX 35, CX 36 and certain reports prepared by SAMI and several other firms. (*See* ALJ's Order of October 4, 1977.)

102. In 1975, the year before Pillsbury acquired Fox, the retail frozen prepared pizza industry had sales of $407 million. In 1976, the year the acquisition took place, the national frozen prepared pizza industry had sales of $463 million. Sixteen percent of total national frozen prepared pizza sales occurred in nine of the local markets where Fox and Totino's competed prior to the acquisition in both 1975 and 1976. (CX 36 *in camera;* CCPF 150-52.) **[29]**

103. In 1976, the year in which the acquisition took place, Pillsbury's Totino's brand ranked third in the national retail frozen prepared pizza industry with 15.4% of sales and Fox ranked eleventh with 1.7% of sales. The acquisition of Fox raised Pillsbury to a 17.1% share of the market. (CX 36 *in camera;* CCPF 178.) The Pillsbury 1976 Annual Report states that Totino's ranked *second* in national market share in both dollars and unit volume. (CX 1, p. 10; CCPF 182.)

104. In 1975, the last full pre-acquisition year, Pillsbury's Totino's brand ranked third in the national frozen food prepared pizza industry with 13.7% of sales and Fox ranked ninth with 2.4% of sales. Thus, Fox and Pillsbury combined had a 16.1% share of the market. (CX 36 *in camera;* CCPF 179.)

105. The acquisition increased the national level of four firm concentration in 1975 market shares from 60.88% to 63.23% and eight firm concentration from 83.49% to 85.84% and increased the national level of four firm concentration in 1976 from 60.80% to 62.53% and eight firm concentration from 83.79% to 85.52%. (CX 36 *in camera;* CCPF 183-84.)

106. Industry leaders' market shares show this trend:

	Top 2 Firms %	Top 3 Firms %	Top 7 Firms %
1973	27.18	39.65	70.74
1974	31.61	45.43	73.51
1975	38.72	51.37	79.50
1976	40.68	53.37	80.74

(CX 55 *in camera;* CCPF 157.)

107. The trend toward concentration probably will continue. Pillsbury's Vice President of Mergers and Acquisitions projected that the top three companies in the frozen prepared pizza industry will capture 60–70% of the national market by 1980. (Levin, Tr. 175.) The Chairman of the Board of Jeno's, Mr. Jeno Paulucci, said that if the present intensely competitive activity of the large companies in the frozen prepared pizza industry continues he believes that the industry will consist of only four or five companies. (Paulucci, Tr. 2431–32; CCPF 159.) [**30**]

108. The Fox acquisition may trigger the acquisition of other frozen pizza companies. It caused Jeno's to consider purchasing other frozen pizza companies, although such a course of action has been postponed by the company pending the outcome of instant litigation. (Barton, Tr. 1401–02, 1432–34; CCPF 200.) The acquisition by Pillsbury of Totino's triggered the sale of Saluto Pizza to General Mills. (DeLapa, Tr. 1200–02; CCPF 201.)

109. Fox was considered by some other manufacturers of retail frozen prepared pizza, including Saluto and Jeno's, to be among their substantial competitors in a number of local markets. (DeLapa, Tr. 1159–60; Barton, Tr. 1461–62; CCPF 204.)

110. Witnesses from all levels of the distribution chain testified that competition in the frozen prepared pizza industry is extremely "tough." (Levin, Tr. 240, 242–43, 238–39; Caron, Tr. 1030; Patterson, Tr. 1766; Moore, Tr. 1812; Dursteen, Tr. 2330; DeLapa, Tr. 1162, 1223; Malkowicz, Tr. 860, 894–95; Urbanowicz, Tr. 1857; RPF 154.)

111. Many factors have radically altered the nature of the industry in recent years. For example:

(a) Applicable government regulations have become more stringent, thereby increasing the difficulty and expense of entering the business. (Francia, Tr. 1556–58; DeLapa, Tr. 1148–55.)

(b) Although it remains possible to enter the business inexpensively, sustained and significant participation now requires high technology. (Pizza, Tr. 748, 766.) The industry is changing from labor intensive to capital intensive. (Caron, Tr. 1018, 1031–32.)

(c) The entry of large national firms (*e.g.,* General Mills, Purex, Quaker Oats, Pillsbury) has made the business intensely competitive with very heavy advertising and promotional activity. (Pizza, Tr. 704; Bard, Tr. 1721-24; DeLapa, Tr. 1084, 1162; Caron, Tr. 1033-34; Rosen, Tr. 1887-88.) [31]

An exchange between complaint counsel and a witness he called, Thomas Caron of Schwan's Sales Enterprises, the maker of "Tony's" pizza, discloses industry changes:

BY MR. BRICKFIELD:

Q. In response to Mr. French's question about the competition being stronger, you stated they were different competitively, and can you tell us what you mean by that?

A. They are different competitors. The competitors that existed not much more than three years ago — they are basically the people that started in the business. And in the process of the last three years, the competitors have changed from individuals with relatively limited resources to being very large companies in the food business, traditionally with considerably more resources. (Caron, Tr. 1051.)

(d) Coupled with these trends is a widespread tendency of major food chains and distributors to replace lower priced pizzas (such as Fox, Lambrecht, G&W and John's) with private-label products of their own. (RX 22; RPF 236.) The implications of this change for a small underfinanced firm like Fox are clear. If small firms are going to have to support their product with extensive promotions and advertising, it gets more difficult to sustain a reasonable profit a small firm can live with; as a result, small frozen pizza manufacturers will disappear. (Rosen, Tr. 1898-99; Francia, Tr. 1557; DeLapa, Tr. 1193; Paulucci, Tr. 2431-32; Chamberlin, Tr. 1513, 1523, 1524, 1532; RPF 239.)

112. As for future trends, as the larger firms expand nationally (Caron, Tr. 1056; Barton, Tr. 1412; Chamberlin, Tr. 1029, 1500-01; Rosen, Tr. 1896-97) and compete for the available retail space (Chamberlin, Tr. 1518; Pizza, Tr. 770; Francia, Tr. 1562-64), small local and regional firms will find it increasingly difficult to enter the business successfully (Chamberlin, Tr. 1525) many such firms will find it increasingly difficult to keep pace and probably will fall by the wayside. (Chamberlin, Tr. 1523-24, 1531-32; Francia, Tr. 1556, 1564-65.) Even large, national firms will choose to exit from the business in search of more profitable business opportunities because frozen pizza is a very low profit margin business, both for Pillsbury

[32] (*see* Prof. Siegfried's profit comparisons, Tr. 2073-77) and for others as well. (DeLapa, Tr. 1223; Dursteen, Tr. 2330; RPF 237.)

113. These changes/trends, however, have not diminished competition. As witness Mr. DeLapa put it, "There are fewer smaller manufacturers, Your Honor, but there are more larger manufacturers because the category has grown so substantially it has now attracted the capital of the multinational companies." (DeLapa, Tr. 1195.) Among the successful recent entrants are such firms as Campbell ("Swanson's"), Heinz ("LaPizzeria"), Banquet, General Host, and Stouffer's. (DeLapa, Tr. 1141-43; Barton, Tr. 1453-54.) The industry now includes among its number many firms having the financial, technical, and marketing skills to survive and prosper, including General Mills (Saluto), RCA ("Banquet"), Beatrice, Campbell, Heinz (LaPizzeria), Stouffer, Quaker Oats ("Celeste"), American Home Products ("Chef Boyardee"), Jeno's, Fairmont Foods ("Creative Crust") Pillsbury ("Totino's" and "Fox") and Purex ("Ellio's"). (Pizza, Tr. 748-50; DeLapa, Tr. 1146-47; Barton, Tr. 1449-51; Rosen, Tr. 1896-97; RPF 238.)

114. Several large firms have entered into the frozen prepared pizza industry in recent years by acquisition. In addition to the entry of Pillsbury in 1975 by acquisition of Totino's, General Mills entered in 1976 by acquiring Saluto (DeLapa, Tr. 1075), Purex entered in 1971 by acquiring Ellio's (Malkowicz, Tr. 858), and Quaker Oats entered in 1969 by its acquisition of Celeste (Chamberlin, Tr. 1472). In addition, other large and well-financed companies have entered by development and marketing of their own product. These include, Pet, Inc., with a product called El Paso Mexican Pizza (Moore, Tr. 1811), Ore-Ida (Heinz) with a product called LaPizzeria (Rowlatt-Smith, Tr. 3732-33). (Note: Heinz also acquired a frozen prepared pizza manufacturer (Baltino) in 1977 (Rowlatt-Smith, Tr. 3748).) In addition, Fairmont Foods entered with a product called Creative Crust (*see* Dursteen, Tr. 2324-25), and Stouffer did so with its French bread style frozen pizza. (MacDonald, Tr. 2920-24; CCPF 156; RPF 168.)

115. There are strong competitors in every area of the country, and there are different sales leaders in each region and local area. (Caron, Tr. 1045; Pizza, Tr. 715; Francia, Tr. 1550; Barton, Tr. 1410; Malkowicz, Tr. 886.) For example, in St. Louis, one of the submarkets alleged in the complaint, there are many different brands of frozen prepared pizza sold and no one brand dominates. (Pizza, Tr. 761; Smith, Tr. 1630; RPF 155.) [33]

116. The intense competition affects sales and distribution of the larger manufacturers as well as of the smaller ones. Large compa-

nies, such as American Home Products (Chef Boyardee brand) and General Mills (Saluto brand) have lost market share in areas while smaller competitors such as Stouffer's Frozen Foods, and Tree Tavern, Inc., have been able to stay in business and to expand if desired. (Roxbury, Tr. 802; DeLapa, Tr. 1087; Stauffer, Tr. 2112; Francia, Tr. 1550; RPF 156.)

117. In determining the price of their product, manufacturers take into account prices of other brands of frozen prepared pizza. They do not significantly consider the prices of other frozen foods. (*See e.g.,* Rowlatt-Smith, Tr. 3762–63.) Manufacturers promote their product against and in response to promotions of frozen prepared pizza by other manufacturers. (*See* Caron, Tr. 1006–08; RPF 60.)

118. Manufacturer-sponsored sales promotions are offered to retailers at different times in different areas and can be limited to one metropolitan area or to a larger region. (Nickel, Tr. 439–40, 498; Roxbury, Tr. 805; Barton, Tr. 1391–92, 1445–46; RPF 108.)

119. Another form of competition in the frozen pizza industry is found in the attempts of suppliers to get more space for their brand in the pizza section of frozen food cases in retail grocery stores. (Francis, Tr. 662–63; Pizza, Tr. 704–05, 707–08; Roxbury, Tr. 809–10; Malkowicz, Tr. 894–95; Caron, Tr. 1003–05; Chamberlin, Tr. 1517–19; CCPF 138.)

120. Manufacturers examine and evaluate competitive conditions (*e.g.,* pricing and promotional allowances) in each local market separately. (Pizza, Tr. 701; CCPF 141.) Local market knowledge is necessary for manufacturers because retail frozen prepared pizza is a very "market particular" product in that customers and the trade in different markets have vastly differing size and flavor preferences. (Carlson, Tr. 575–78; Pizza, Tr. 711–12; Malkowicz, Tr. 879; Chamberlin, Tr. 1479–80.) Pittsburgh is a "cheese" market (Carlson, Tr. 592), but cheese topped frozen pizza does not sell well in St. Louis. (Patterson, Tr. 1782.) Kansas City is a "hamburger" market; General Mills was unsuccessful in entering the Kansas City market until it developed a hamburger pizza. (DeLapa, Tr. 1086–88.) Sausage pizza is the leading variety in St. Louis, even though it is close to the Kansas City "hamburger" market. (Smith, Tr. 1641.) [34]

121. Promotional allowances vary from market to market. (Carlson, Tr. 536–37; Francis, Tr. 669–70; Caron, Tr. 1018, 1034; DeLapa, Tr. 1218–20; Carpenter, Tr. 1336.) Different markets require different promotional and introductory programs because of the type of competitive activity in each market. (DeLapa, Tr. 1084–85; Barton, Tr. 1460–61.) Houston, Texas, is known as a free-goods market (*e.g.,*

one case free to a reseller with five purchased). (Carpenter, Tr. 1340–41; CCPF 142.)

122. Manufacturers concern themselves with and gather information regarding local and regional competitive conditions in the frozen prepared pizza business because of the distinct nature of competition and consumer preferences. (Nickel, Tr. 494.) Food brokers are relied upon to provide to frozen prepared pizza manufacturers regular, monthly, often weekly, information on competitors' prices, promotional activity, and new product introductions in each local market. (Carlson, Tr. 536–37, 548; Pizza, Tr. 703–04; Walling, Tr. 1277–80; Carpenter, Tr. 1334–36; Chamberlin, Tr. 1481–82; Patterson, Tr. 1746–48, 1753–54; Mosley, Tr. 1819–20.) Manufacturers also monitor local market activity by regular reviews of SAMI reports on each local market. (Pizza, Tr. 689; Malkowicz, Tr. 864–65; CCPF 144.)

123. Frozen prepared pizza manufacturers often tailor their promotional allowances and advertising efforts in a particular local market in response to promotions offered or advertisements run by one or more of their competitors in that local market. (As to promotions: Nickel, Tr. 440; Pizza, Tr. 709–10; Malkowicz, Tr. 861–62; Walling, Tr. 1298, 1300; Carpenter, Tr. 1337; Barton, Tr. 1445–46; As to Promotions and Advertising: DeLapa, Tr. 1084, 1112–13; CCPF 149.) [35]

Geographic Areas of Competition in the Frozen Prepared Pizza Industry

124. The parties agree that the United States as a whole is a relevant geographic market—the section of the country—within which Pillsbury's acquisition of Fox should be examined to determine the potential impact of the merger on competition (CCPF 120; RPF 79) but complaint counsel also contend that certain local metropolitan areas are relevant sections. (Complaint and Answer, ¶ 16; CCPF 121–23.)

125. Manufacturers of frozen prepared pizza in the United States have widely disparate distribution patterns. For example, one distributes coast to coast, but not border to border. (Pizza, Tr. 681.) Another distributes product in the States of Virginia, Colorado, Utah, Arizona, California and Hawaii. (Dursteen, Tr. 2337, 2338.) Yet another, having sales as far south as Miami, Florida, supplies product to that area from as far north as Duluth, Minnesota. (Malkowicz, Tr. 910; Carpenter, Tr. 1353.) Still another supplies pizza on a national basis, including Alaska, from a single plant in Salina, Kansas. (Miller, Tr. 977; Caron, Tr. 1023–24.) Even a small manufac-

turer like "Tree Tavern" can and does distribute product in three areas east of the Allegheny Mountains, Puerto Rico, and the U.S. Virgin Islands. (Francia, Tr. 1541-42; RPF 81.)

126. Many manufacturers are currently shipping product long distances and distribute product in a substantially nationwide pattern. Some manufacturers selling on a national basis ship frozen prepared pizza made at a single plant location. (Pizza, Tr. 679, 681, 731-34; Malkowicz, Tr. 898-901; Carpenter, Tr. 1353; Barton, Tr. 1434, 1440; Chamberlin, Tr. 1491-92; MacDonald, Tr. 2920, 2952-53; Cady, Tr. 3330; RX 1; RX 3; RPF 82.)

127. Transportation costs do not prevent frozen prepared pizza manufacturers who have only one or two manufacturing facilities from selling frozen prepared pizza anywhere in the United States. (Pizza, Tr. 734; Roxbury, Tr. 833; Barton, Tr. 1440; Cady, Tr. 3330-31; Malkowicz, Tr. 891-92; RX 7; RPF 89.) [36]

128. Buyers of pizza, located anywhere in the United States, can turn to manufacturers, located anywhere in the United States, for competitively priced products. (Cady, Tr. 3330, 3412-18, 3421-23, 3436-37; RPF 90.)

129. The manufacturers of Ellio's (Purex Corporation), Saluto (General Mills) and Stouffer's pizza not now in national distribution have present plans to achieve such distribution. (Malkowicz, Tr. 857, 891-92; DeLapa, Tr. 1072, 1134-35; Bard, Tr. 1704-05; MacDonald, Tr. 2921.) Ellio's (Purex) plans to expand its distribution to a nationwide level using two plants located 17 miles apart. (Malkowicz, Tr. 891-92; RPF 84.)

130. The only limitation on Pillsbury's geographical distribution of pizza has been its production capacity, which is insufficient to meet demand. (Francis, Tr. 612-20, 655; CX 27, p. 2; CX 7, p. 13; CX 6, p. 8.) This shortage in capacity is the reason that Pillsbury has not entered the trade areas of New England, New York and Los Angeles. (Nickel, Tr. 472; RPF 86.)

131. Since April 1976, utilizing one plant in Ohio, Ore-Ida, a subsidiary of H.J. Heinz Company (LaPizzeria brand), expanded its sales of frozen prepared pizza to the eleven cities or areas in the order listed: (1) Denver, (2) Chicago/Milwaukee, (3) Kansas City, (4) Des Moines, (5) Peoria, (6) Wichita, (7) Baltimore/Washington, (8) New Orleans, (9) Phoenix, (10) Tucson, (11) "the majority of the Northeast." (Rowlatt-Smith, Tr. 3767-68; RPF 87.)

132. Manufacturers of frozen prepared pizza recognize local grocery distribution areas as distinct and separate markets. (Boyce, Tr. 357-58, 362; Malkowicz, Tr. 873; Caron, Tr. 1002-03, 1043; DeLapa, Tr. 1099-1100; CCPF 135.)

133. Local marketing areas in which Fox and Totino's competed prior to the acquisition include: Houston, Dallas, and Lubbock, Texas; Tulsa, and Oklahoma City, Oklahoma; St. Louis, Kansas City, and Springfield, Missouri; Memphis, Tennessee; Little Rock, Arkansas; Atlanta, Georgia; North and South Carolina; Louisiana; Mississippi; Omaha, Nebraska; Montgomery and Birmingham, Alabama; and Denver, Colorado. (Boyce, Tr. 393; CCPF 122.) [37]

134. Localized geographic markets in which Pillsbury's Totino's and Fox competed prior to the acquisition and for which there are SAMI market share statistics available (CX 36 *in camera*) are:

1. Atlanta, Georgia
2. Charlotte, South Carolina
3. Dallas/Ft. Worth, Texas
4. Houston, Texas
5. Kansas City, Missouri
6. Memphis/Little Rock, Tenn., Ark.
7. Oklahoma City/ Tulsa, Oklahoma
8. Omaha, Des Moines, Neb. & Iowa
9. St. Louis, Missouri

(CCPF 123)

135. Forty-four percent of the total retail sales of Fox frozen prepared pizza sales, excluding private label sales, occurred in these nine market areas and 25% of the total retail sales of Totino's Frozen prepared pizza sales occurred in these markets in 1975 and 1976. (CX 36 *in camera;* CCPF 124.)

136. Industry recognized, local grocery distribution markets result from concentrations of food brokers, grocery buyers and warehouses. (DeLapa, Tr. 1218–20.) Local markets are "hubs of business"—population centers (Follansby, Tr. 1625), although they are not conducive to exact delineation by metes and bounds. (Caron, Tr. 1045.) They are, however, identifiable areas. (Nickel, Tr. 450–51.)

137. Usually, brokers acting as exclusive sales agents represent manufacturers within established territories. (Carlson, Tr. 586–87; Pizza, Tr. 702; Malkowicz, Tr. 884; DeLapa, Tr. 1096–97; Barton, Tr. 1391; Chamberlin, Tr. 1472–73.) Manufacturers of frozen prepared pizza often define local grocery distribution markets in terms of the boundaries of local food broker territories. (Pizza, Tr. 688; Carpenter, Tr. 1332, 1355, 1360; Barton, Tr. 1392; Chamberlin, Tr. 1473; CCPF 125.) [38]

138. The territory of food brokers is based, primarily on th location of retail food chain buying offices and wholesalers (DeLap

Tr. 1213-14; Barton, Tr. 1392; CCPF 127) and correspond to population centers, *e.g.,* St. Louis, Houston, or Kansas City, have been long-established, and are well-recognized in the grocery distribution trade. (Boyce, Tr. 353; Walling, Tr. 1328-29; Chamberlin, Tr. 1472-73; Patterson, Tr. 1738-39; CCPF 128.)

139. While the precise boundaries of various food broker territories in a given area may not coincide, they are generally similar (Carpenter, Tr. 1341; Mosley, Tr. 1824; Rosen, Tr. 885) and while differing slightly on the fringes, they share a core "city," *e.g.,* St. Louis, Houston, etc. (Follansby, Tr. 1625; CCPF 129.)

140. Food brokers "follow" retail grocery distribution patterns and service, *i.e.,* check displays, price markings, etc., even if a store of a chain is outside the broker's area of primary responsibility. (Pizza, Tr. 764, 777; Walling, Tr. 1291, 1315, 1328-29; Francia, Tr. 1544-45; RPF 94.)

141. Thus pizza sold by brokers within their areas of primary responsibility may be distributed by the purchasing reseller into the area of other brokers. The trade refers to this as competitive "spillover" or "overlap." (Nickel, Tr. 448; Pizza, Tr. 741, 764; Follansby, Tr. 1612; Walling, Tr. 1312-16, 1321, 1328-29; Barton, Tr. 1455; Francia, Tr. 1544-45; Coles, Tr. 1590; Patterson, Tr. 1758; Mosley, Tr. 1822; RX 10; RPF 95.)

142. Pizza distribution patterns and broker territories may or may not correspond to territories outlined by SAMI for its purposes. (Carlson, Tr. 571-72; Pizza, Tr. 742; Miller, Tr. 993; Caron, Tr. 1026; DeLapa, Tr. 1121-22; Patterson, Tr. 1742; Moore, Tr. 1806-07; Mosley, Tr. 1816-17; Barton, Tr. 1395-98; Rosen, Tr. 1883-84; Chamberlin, Tr. 1473-74; RPF 101.)

143. Some manufacturers have sales areas completely outside SAMI marketing areas. Others have sales areas which are partly within and partly outside such areas. SAMI determined that it would not be possible to encompass within the geographic boundaries of its areas all stores served by each reporting warehouse, because the listribution patterns of no two warehouses are precisely the same. CX 54, p. 8; Caron, Tr. 1027-28; DeLapa, Tr. 1182; Follansby, Tr. 624; RX 4; RPF 102.) [39]

The Plant Tour and Taste Test Conducted

144. As mentioned above (p. 9), a tour of the Fox Deluxe Pizza Co. ant in Joplin, Missouri, was taken. Frozen prepared pizza is ınufactured there in the following manner which is typical: (1) ıgh is mixed, rolled out and cut into individual crusts; (2) the sts are then passed through an oven where they are partially

baked and cooled; (3) a tomato sauce and a meat or other topping is prepared separately and readied to be placed on the pizza; (4) the crusts are fed through a tomato sauce applicator; (5) cheese and some other toppings may also be applied either mechanically or by hand; (6) the fully garnished pizzas are then frozen in a blast (very quick-acting) freezer, packaged for sale, scanned electronically for foreign particles of metal and stored in a freezer until sold. (Balster and Spencer, Tr. 2150–2218; RPF 57.)

145. Also as a part of this proceeding, a taste test or competitive cutting, as is the custom in the trade, was held in an attempt to determine the similarities and differences in the various forms of pizza. (*See* RX 27 through RX 36, RX 27A through RX 36A, Tr. 2457–2538.) Pizza which came initially in a grocery shelf-stable, refrigerated, or frozen form, as well as pizzeria pizza was prepared according to package instructions or heated in the Pillsbury test kitchens. (*See* RX 24A – RX 36B.) The pizza samples served were not identifiable by type by the ALJ regardless of whether they initially were frozen, freshly baked or reheated, refrigerated, or grocery shelf-stable product. An exhibit (RX 24) shows the types tasted. It may be of interest that the ALJ only made one correct guess as to the type being tasted.

146. For a discussion as to the desirability and propriety of the trier of fact taking a tour of the Fox frozen prepared pizza manufacturing facility in Joplin, Missouri, and participating in the taste test in the Pillsbury kitchens in Minneapolis, Minnesota, *see* "Demonstrative Evidence," "McCormick on Evidence," "West Publishing Company, 2 ed., pp. 537–539." *Also see,* "Autoptic Proference," "Wigmore on Evidence," Chadbourn Revision, n.9, p. 388 and pp. 391–94. **[40]**

Barriers To Entering the Frozen Prepared Pizza Industry

147. A new plant designed to augment the production require ments of Pillsbury's Totino's brand pizza operation (which alread has a manufacturing facility at Fridley, Minnesota) would cost $1 million. (Levin, Tr. 239–40.) The cost of leasing a frozen prepar pizza production facility also is high: Purex paid $3 million to lea and improve its frozen prepared pizza facility which has a sin production line. (Malkowicz, Tr. 927; CCPF 164–165.)

148. In order to effectively compete in the frozen prepared p business, a company must advertise and promote extensi Economies of scale in advertising and production are necessa enter and become an effective competitor given the magnitude o other companies in the retail frozen prepared pizza business. (I

Tr. 248; DeLapa, Tr. 1084, 1103–04; Chamberlin, Tr. 1525–29; Horsch, Tr. 2710–11; CCPF 170.)

149. The expenditures for advertising and promotion are greater in gaining distribution of frozen prepared pizza than in any other frozen food category. (DeLapa, Tr. 1084.) Merely developing a good tasting product is not sufficient to enter the industry without extensive advertising and promotion. (Patterson, Tr. 1750–51.) Pillsbury recognized that expanding into new geographic areas, "dominated by well-established brands . . . will be extremely costly and represent[s] a drain on Divisional profit until the Totino's brand is well-established." (CX 2, p. 3, *in camera;* CCPF 172.)

150. The time period between entering the retail frozen pizza business and earning a normal return is long, and, therefore, a new entrant must be able to sustain losses over an extended interval. (Cady, Tr. 3379–81; CX 2, p. 96 *in camera;* CCPF 174.)

151. It is possible, though, to get into the business on a small scale with a total investment of about $50,000. (Stauffer, Tr. 2110; RPF 59.) [41]

Discussion

Elements of Section 7 of the Clayton Act

Section 7 (15 U.S.C. 18) provides that no corporation engaged in commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital of another corporation engaged also in commerce, where in any line of commerce (the product market), in any section of the country (the geographic market), the ›ffect of the acquisition may be substantially to lessen competition, r to tend to create a monopoly.

Both Pillsbury and Fox were corporations engaged in commerce 'indings 1 and 2). That having been established, "determination of ɘ relevant product and geographic market is 'a necessary predi- e' to deciding whether a merger contravenes the Clayton Act." *ited States* v. *Marine Bancorporation, Inc.,* 418 U.S. 602, 618 '4); *Brown Shoe Co.* v. *United States,* 370 U.S. 294, 324 (1962); *'ed States* v. *E.I. du Pont de Nemours & Co., et al.,* 353 U.S. 586, 1957).

The Product Market/The Line of Commerce

ıtification of the product market(s) affected by the acquisition first step to be taken in a Section 7 case in determining ·r a substantial lessening of competition has occurred or y will occur as a result of the acquisition. *Brown Shoe Co.,* *supra,* 370 U.S. at 324. In that leading case, the Supreme Court said that while there may be broad product markets whose outer boundaries "are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it . . .," there also may be "well defined submarkets" within the broader market which in themselves constitute product markets for antitrust purposes. Thus, men's, women's and children's shoes were held to be economically significant submarkets within the shoe industry — the broad product market. 370 U.S. at 325.

The court described seven factors which led it to distinguish the submarkets:

industry or public recognition of the submarket as a separate economic entity, the product's peculiar characteristics and uses, unique production facilities, [42] distinct customers, distinct prices, sensitivity to price changes, and specialized vendors . . . 370 U.S. at 325.

Thus, in cases decided subsequently such as *United States* v. *Aluminum Co. of America* (Alcoa-Rome), 377 U.S. 271 (1964), separate aluminum and copper submarkets were found to exist in the wire and cable industry and a separate paper insulated power cable submarket was found in *United States* v. *Kennecott Copper Corp.* (Kennecott), 231 F. Supp. 95, 98-100 (S.D.N.Y. 1964), *aff'd per curiam,* 381 U.S. 414 (1965). Even before *Brown Shoe,* it was held in *U.S.* v. *Bethlehem Steel Corp.,* 168 F. Supp. 576, 593-95 (S.D.N.Y. 1958), that while the iron and steel industry was the broad product market, ten specific items (*e.g.,* hot rolled sheets, track spikes, electricweld pipe, oil field equipment and supplies) comprised identifiable product submarkets as well.

Decisions such as *Alcoa-Rome, Kennecott,* and many others which came after *Brown Shoe* have made it clear that not all or even most of the seven factors need to be present before a valid submarket for Section 7 purposes may be found to exist. *Liggett & Myers, Incorporated* v. *FTC,* 567 F.2d 1273, 1274-5, (4th Cir. 1977); *United States* v. *Phillipsburg National Bank & Trust Co.,* 399 U.S. 350, 359-60 (1970); *United States* v. *Continental Can Co.* (Continental Can), 378 U.S. 441, 456-57 (1964); *Columbia Broadcasting System, Inc.* v. *FTC,* 414 F.2d 974, 979 (7th Cir. 1969), *cert. denied,* 397 U.S. 907 (1970); *General Foods Corp.* v. *FTC,* 386 F.2d 936, 941 (3rd Cir. 1967); *Reichold Chemicals, Inc.,* Dkt. 9076, p. 63, Initial Decision, Commission Opinion, slip copy, dated February 22, 1978 [91 F.T.C. 246]; *U.S.* v. *Mrs. Smith's Pie Co.,* 1977-1 CCH, Trade Cas. ¶61,518 (E.D. Pa. Nov. 19, 1976) at 72,021-3.

Counsel for Pillsbury contends that only the broad market, pizza be it prepared frozen (*e.g.*, completely prepared except for heating), refrigerated (*i.e.*, requiring a combination of various components plus heating), shelf-stable (*i.e.*, dry and requiring mixing of ingredients and the combination of components plus cooking) or carry-out from a pizzeria restaurant (*i.e.*, ready-to-eat), is the relevant line of commerce. He also suggests that the market includes such products as frozen TV dinners and other frozen entrees, other carry-out foods, etc. (Respondents' Brief, pp. 8-13.) [43]

I do not agree, even though in an appropriate case the broad market — pizza in its various forms — might be examined as the relevant line of commerce. *See Continental Can, supra,* 378 U.S. at 456-58. There is ample, convincing evidence to establish that frozen prepared pizza is the relevant product market and that this case is not appropriate for an examination of the additional products counsel for Pillsbury proposes.

The evidence here shows that frozen prepared pizza is recognized by the food industry as being separate and distinct. The manufacturers, as do the brokers normally employed for distribution of frozen prepared pizza to resellers, so consider it. (Findings 66, 67, 70-73.) In addition, producers/manufacturers of frozen prepared pizza look at the activity/business operations of other such producers in deciding their competitive actions. (Findings 58-62.) There is an association of frozen prepared pizza manufacturers. (Finding 54.) Further, frozen prepared pizza has peculiar characteristics due to its manner of preparation, state of completion and manner of preservation. Also frozen prepared pizza is sensitive primarily to changes in the price of other frozen prepared pizza. (Findings 38-41, 50, 57, 68, 117.) Lastly, frozen prepared pizza is made on machinery, sometimes custom-designed, which is different from that used to make other types of pizza by producers who concentrate on the manufacture of frozen prepared pizza as distinguished from pizzeria, shelf-stable and refrigerated pizza. (Findings 44, 51, 55.) It also is appropriate to mention that simply because the administrative law judge only guessed right once in the taste test (Finding 145) the fact is of no consequence in determining the relevant product market in this case.

The frozen prepared pizza market is "sufficiently inclusive to be meaningful in terms of trade realities." *Crown Zellerbach Corporation* v. *FTC,* 296, F.2d 800, 811 (9th Cir. 1961) and it is proper to consider frozen prepared pizza as the relevant line of commerce in connection with determining whether the acquisition of Fox by Pillsbury violated Section 7. [44]

2. The Geographic Market/The Section of the Country

The section(s) of the country or geographic market(s) one must examine in order to determine whether an acquisition has or probably will substantially lessen competition is(are) identified in much the same way as the product market. Thus, in *Brown Shoe, supra,* 370 U.S. at 336–37, the Supreme Court said that the "criteria to be used in determining the appropriate geographic market are essentially similar to those used to determine the relevant product market. . . . The geographic market selected must . . . both correspond to the commercial realities of the industry and be economically significant. . . . [A]lthough the geographic market in some instances may encompass the entire Nation, in some other circumstances, it may be as small as a single metropolitan area."

Particularly clear from *Brown Shoe* and other precedents is that in a case such as this the section of the country to be examined need not be marked off in metes and bounds. *United States* v. *Pabst Brewing Co.,* 384 U.S. 546, 549 (1966); *E.I. du Pont & Co., supra,* 351 U.S. at 395. In connection with identification of regional markets, in *Philadelphia National Bank,* 374 U.S. at 360 n.37 (1963), the Supreme Court said:

> . . . there is still some artificiality in deeming the four county area the relevant 'section of the country' so far as businessmen located near the perimeter are concerned. But such fuzziness would seem inherent in any attempt to delineate the relevant geographical market.

Also see United States v. *Connecticut National Bank,* 418 U.S. 656, 669–70 (1974), where the Court said that it is the Government's role to come forward with evidence "delineating the rough approximation of localized banking markets mandated by *Phildelphia Bank, supra,* and *Phillipsburg National Bank, supra.*"

The effects of an acquisition have been considered by the Supreme and lower Courts with reference to both broad geographic markets and submarkets within the broad area, in basically the same manner as in the case of product markets. *United States* v. *Kimberly-Clark Corp.,* 264 F. Supp. 439, 455–56 (N.D. Cal. 1967); *United States* v. *Bethelehem Steel Corp., supra,* 168 F. Supp. at 601–02. [45]

In *Marine Bancorporation, supra,* 418 U.S. at 620–21, where potential rather than, as here, horizontal competition was involved, the Supreme Court held that "without exception the Court has treated 'section of the country' and 'relevant geographic market' as identical, and it has defined the latter concept as the area in which the goods or services at issue are marketed to a significant degree by the acquired firm." In commenting on the "section of the country" holding of the Court in *Pabst Brewing, supra,* 384 U.S. at 550–51, the Court said in *Marine Bancorporation* in footnote 20:

> Some of the Court's language in *Pabst* suggests that the Government may challenge a merger under § 7 without establishing any relevant geographic market. . . . But Pabst in reality held that the Government had established three relevant markets in which the acquired firm actually marketed its products—a single State, a multistate area, and the Nation as a whole. . . . And in that case the acquiring firm was an actual competitor of the acquired firm in all three relevant geographic markets. . . . Thus while *Pabst* stands for the proposition that there may be more than one relevant geographic market, it did not abandon the traditional view that for purposes of § 7 "section of the country" means "relevant geographic market" and the latter concept means the area in which the relevant product is in fact marketed by the acquired firm.

Under these criteria, in this case both the United States as a whole and those regional areas of the United States in which Pillsbury and Fox competed could be examined as the relevant sections of the country. As noted, counsel agree on the national geographic market but disagree as to whether local geographic markets also should be considered.

Complaint counsel contend that several regional areas comprised of metropolitan centers of the United States are also relevant sections of the country. (Complaint ¶ 19.) They may be but the evidence does not establish the fact sufficiently. For example, there is no evidence that customers are limited by circumstances or limit themselves to sellers located in any meaningful geographic area other than the United States as a whole. Even if the proposed/alleged regions were accepted as relevant geographic markets, the evidence does not establish that any of them is effectively insulated from outside competitive forces which the Commission has said is an important distinguishing characteristic. *Jim Walter Corp.*, Dkt. 8986, 3 CCH TRR ¶ 21,379 at 21,316, December 20, 1977 [90 F.T.C. 671].

It is well established that Section 7 of the Clayton Act does not require precise mathematical certainty in the ascertainment of market size and market share, *Brown Shoe, supra,* 370 U.S. at 341–42, n.69, but more is needed than we have here to support a conclusion as to regional markets. [46]

The U.S. District Court, in *U.S.* v. *Mrs. Smith's Pie Co., supra,* 1977-1 CCH Trade Cas. relied on SAMI statistics to make a determination as to the national market shares concluding, and I agree, that SAMI data/evidence is reasonable, credible and reliable for such use at ¶61,518 p. 72,017.

In 1976, Pillsbury and Fox competed in selling frozen prepared pizza in thirteen, widespread states, from Alabama to Colorado

(Finding 133). Frozen prepared pizza is distributed nationally. The major firms compete with others throughout the United States (Findings 126-131). These facts warrant considering the nation as a whole as a relevant geographic market. *See* Commission Opinion in *Jim Walter Corporation, supra,* Dkt. 8986, 3 CCH TRR at 21,313-16. This conclusion is reinforced by the fact that the parties agree on the Nation as the relevant geographic market. (Finding 124).

Even though Pillsbury and Fox did not actually sell their frozen prepared pizza in every state, there are numerous precedents to the effect that a national market may be considered in the circumstances obtaining here. *See FTC* v. *Procter and Gamble Co.,* 386 U.S. 568, 571-72 (1967); *Pabst, supra,* 384 U.S. at 549-51; *A.G. Spalding & Bros., Inc.* v. *FTC,* 301 F.2d 585, 607 (3d Cir. 1962); *Kimberly-Clark, supra,* 264 F. Supp. at 454-58.

In *Kennecott Copper Corp.,* Dkt. 8765, 78 F.T.C. 744 at 917-18 (May 5, 1971), the Commission said that a national market existed for coal even though the acquired firm (Peabody Coal Company) sold principally in the North and South Central States and there was no evidence of sales in the Northeast, Mid-Atlantic or Northwestern States, *aff'd,* 467 F.2d 67 (10th Cir. 1972), *cert. denied,* 416 U.S. 909 (1974), *rehearing denied,* 416 U.S. 963 (1974). *Also see United States* v. *Jos. Schlitz Brewing Company,* 253 F. Supp. 129 at 134-35 (N.D. Cal. 1966).

Consequently, and as is alleged in the complaint (¶ 16), the United States as a whole is the relevant section of the country for consideration in this case. [47]

3. Market Concentration

The Congress made it clear that its primary concern when the Clayton Act was amended was to forestall, insofar as possible, reductions in competition in all lines of commerce by keeping a large number of small competitors in business. *United States* v. *Von's Grocery Co.,* 384 U.S. 270, 275 (1966). More recently, the Supreme Court in *Phildelphia National Bank, supra,* 374 U.S. at 363, as quoted in *United States* v. *General Dynamics Corp.,* 415 U.S. 486 at 497 (1973), said:

> This intense congressional concern with the trend toward concentration warrants dispensing, in certain cases, with elaborate proof of market structure, market behavior, or probable anticompetitive effects. Specifically, we think that a merger which 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. [Emphasis added]

In Section 7 cases market shares are the primary indicia of market power, but it is also necessary to examine the structure, history, and probable future of the particular market. *U.S.* v. *Continental Can Co.*, 378 U.S. at 458 (1964). (RPF p. 124.)

Competition in the manufacture of frozen prepared pizza is intense and probably will continue to be so. (Findings 107, 110-13, 115.)

In *Stanley Works* v. *FTC*, 469 F.2d 498, 504 (2nd Cir. 1972), *cert. denied*, 412 U.S. 928 (1973), the court said that the cabinet hardware industry was concentrated because the 4-firm percentage of market was 49 percent to 51 per cent. To the same effect, in *Industrial Organization*, Professor Joe Bain says that a market in which the 4-firm percentage is 50 percent reflects high-moderate concentration (p. 31, 2d ed. 1968). After Pillsbury acquired Fox 4-firm concentration was 63.23% in 1975 and 62.53% in 1976. (Finding 105.) However, the merger in this proceeding does [48] not fall within the class of horizontal mergers, ordinarily subject to challenge under the Department of Justice Merger Guidelines. (1 Trade Reg. Rep., ¶4510 at 6884.) Neither in 1976 nor in 1975 did Fox, with its 1.7% and 2.4% market share (see next paragraph) come up to the Department's criteria of the acquired firm having 2% or more if the acquirer had at least 20% (1976) or less than 2% if the acquirer had 25% (1975). (Findings 103, 104.)

The evidence here shows that based on SAMI data national 4-firm and 8-firm concentration was about 62% and 84% respectively in 1976 (Finding 105) and that nationally Fox and Pillsbury had market shares of: Fox 1.7% in 1976 and 2.4% in 1975; Pillsbury 17.1% in 1976 and 16.1% in 1975. (Findings 103, 104.)

Counsel for Pillsbury questions the use of the SAMI data offered by complaint counsel to show these market shares (RB, pp. 24-35) but I am convinced that it is probative evidence in this case. Even though SAMI data is not as precise as some other sources of such information might be (*e.g.*, a Commission Section 6(b) survey) industry member reliance on it persuades me that it is more than adequate for our purposes. This is because the data provides a sufficiently reliable indication of the market shares of various brands of frozen prepared pizza due to SAMI's extensive coverage of the warehouses through which frozen prepared pizza travels in reaching the retailer. Even if it is possible to point to technical flaws in the compilation of industry statistics, the Supreme Court has held that "precision in detail is less important than the accuracy of the broad picture presented." *Brown Shoe, supra*, 370 U.S. at 342 n.69.

Although the SAMI data lack precision in detail when compared with what other techniques for measuring market shares might provide, the SAMI data is probative evidence. Certainly those most qualified, the businessmen concerned with sales of frozen prepared pizza — including Pillsbury — say so by subscribing to the service and relying on it. (Findings 79–83, 85, 95–97.)

The Commission also has said there is no requirement that the exact size of a product market need be shown in a Section 7 case. *Papercraft Corp.,* Dkt. 8779, 78 F.T.C. 1352, 1405–06 (1971), *modified and aff'd,* 472 F.2d 927 (7th Cir. 1973). The SAMI data amply present the "picture" of the sales of frozen prepared pizza in the Nation — the relevant section of the country which has been shown to exist. [49]

As a matter of first impression, this case does appear to be governed by the principles that (1) where there has been a "history of tendency toward concentration in the industry," tendencies toward further concentration "are to be curbed in their incipiency." *Continental Can, supra,* 378 U.S. at 461, citing *Brown Shoe, supra,* 370 U.S. at 345–46, and (2) where "concentration is already great the importance of preventing even slight increases in concentration and so preserving the possibility of eventual deconcentration is correspondingly great." *Philadelphia National Bank, supra,* 374 U.S. at 365 n.42. As a predicate, however, each of these cases had the fact that a *substantial* actual or probable lessening of competition had or would occur. That predicate is missing here. Here, there is convincing evidence that the acquisition did not, and probably will not, result in a substantial lessening of competition. This evidence is discussed under the caption "Competitive Effects." As to the importance of considering such evidence, *see* the Commission's Opinion in *Coca-Cola,* Dkt. 8855, p. 87, April 7, 1978 and reference there to the *Jim Walter* opinion, *supra.*

4. Ease of Entry

Counsel for Pillsbury presented evidence to show that there are no significant barriers to entry into the frozen prepared pizza industry because (1) a plant making frozen prepared pizza can be constructed for very little money or even started in a garage, (2) technological requirements are minimal, (3) the machinery needed is available at reasonable prices, (4) start-up advertising by a small entrant is not important in the industry, (5) small firms do well, and (6) there are ready means of distribution open to new entrants. The evidence as to difficulty of entry, however, (Findings 147–151) outweighs that presented by counsel for Pillsbury. Although I agree with the position of counsel for Pillsbury to the effect that the evidence he presented is germane to questions as to the various aspects of an acquisition, including the probability of adverse competitive effects, that does not negate the fact that in this acquisition, competition between Pillsbury and Fox in a number of sections of the country was eliminated.

Most persuasive however is the fact that ease of entry in and of itself is not an effective defense to a charge that competition has been eliminated. In *Ekco Products Co.,* Dkt. 8122, 65 F.T.C. 1163, at 1208 (1964), *aff'd,* 347 F.2d [50] 745 (7th Cir. 1965), the Commission said:

> . . . where the merger's effects on competition are those prescribed by Section 7, its illegality cannot be overcome by a showing of ease of entry. . . . Ease of entry may, to be sure, cause the market power of established firms to be eroded by the advent of significant new competitors; but that is likely to be at best a long-term affair. . . . In short, the absence of high entry barriers cannot be depended upon to ensure effectively competitive conditions. . . . [and] a merger that has been proved to be so anticompetitive as to violate Section 7, even apart from difficulty of entry into the market, cannot be defended on a mere showing of absence of high entry barriers.

See Bok, *Section 7 of the Clayton Act and the Merging of Law and Economics,* 74 Harvard L. Rev. 226–260 (1960). . . . *Cf.* Bain, Barriers to New Competition 189 (1956); Bain, Industrial Organization 425 (1959).

Also see American Brake Shoe Co., Dkt. 8622, 73 F.T.C. 610, 684 (1968).

In a "horizontal" Section 7 case, the focus is on the existing and future *competition* affected by the firms involved in the merger rather than on the potential for additional competition provided by new entrants into the industry. Thus, the contentions of counsel for Pillsbury regarding ease of entry have not been persuasive in deciding this case but his arguments as to the probable competitive effects have been convincing.

5. Competitive Effects

A basic premise of Section 7 is that competition will be most vital when there are many sellers, none of which has any significant market share. *Philadelphia National Bank, supra,* 374 U.S. at 363; *Alcoa-Rome, supra,* 377 U.S. at 289. The *ultimate* question to be addressed is [51] whether the acquisition/merger has or probably will *substantially* lessen competition in the relevant product and geographic markets. Section 7 was particularly directed against elimination of horizontal competition which was significant and would probably continue to be so in the future. And it has been recognized for a long time that the policy underlying the Section "is that corporate growth by internal expansion is socially preferable to growth by acquisition." *Philadelphia National Bank, supra,* 374 U.S. at 370; *accord, Ekco Products, supra,* 347 F.2d 745, at 752.

Pillsbury and Fox were competitors in the frozen prepared pizza industry and Pillsbury clearly had an appreciable market share nationally. Fox did not. (Pillsbury *13.7%;* Fox *2.4%* in 1975.) (Finding 104.) The acquisition of Fox by Pillsbury did eliminate an independent competitor with the result that the buying options available to reselling and other purchasers of frozen prepared pizza were reduced by one due to Fox having been eliminated as an independent source of supply. (Findings 34, 102.) Even so, the acquisition did not *substantially* lessen competition and probably will not do so in the future.

The Supreme Court has ruled that acquisitions of competitors with even lower industry rankings than those of Pillsbury and Fox are illegal. One example, is *Brown Shoe, supra,* where the combined market share was over 5 percent, 370 U.S. 341–43. In *Alcoa-Rome, supra,* 377 U.S. at 271, acquisition of the ninth ranked firm, with 1.3 percent of the aluminum conductor market, *by the market leader* with a 27.8 percent market share was found to be unlawful. Similarly, a merger between the *sixth and seventh* ranked firms, Blatz with 5.84 percent and Pabst with 5.48 percent, respectively, of the three-state beer market in *Pabst, supra,* 384 U.S. at 551–52, violated Section 7. Also, with a combined market share of 8.9 percent, a merger between the *third-ranking firm* with 4.7 percent and the *sixth-ranking firm* with 4.2 percent of the retail grocery market in the Los Angeles area was held in *Von's Grocery, supra,* 384 U.S. at 281, to violate Section 7. [52]

Instead of growing by expanding internally with the possibility of market deconcentration, Pillsbury combined with Fox and if the competition involved were different a violation of Section 7 would have resulted. The merger of Pillsbury and Fox was decided upon to solve the pressing production problem which Pillsbury had and enabled Pillsbury to more nearly meet its production needs and most important from the standpoint of Section 7 to enter into competition in an already concentrated industry in new geographic areas which Fox had been unable to enter. (Findings 35, 130, 149.) The acquisition created more jobs in the Fox production plant (Finding 14), upgraded the physical condition of those facilities through substantial investment of capital (Finding 15), and made for a more viable, intensive, competitive situation in the frozen prepared pizza industry than would have been the case if Fox had continued as a separate entity. (Findings 111, 112.) Consequently, the acquisition did not and probably will not have the substantial adverse effects on competition which the Congress was addressing when Section 7 was enacted in 1914 and amended in 1950.

Complaint counsel met prima facially, the burden of proving that the effect of the acquisition would be substantially to lessen competition. He showed this by establishing that the Nation and that frozen prepared pizza are the relevant markets and then introducing statistical evidence to show the market shares held by the parties and other industry leaders. *But* such statistical evidence has never constituted more than "*prima facie*"proof of a violation of Section 7. *Jim Walter Corp.,* Commission Opinion in Dkt. 8986, 3 CCH TRR ¶ 21,379, p. 21,320, Dec. 20, 1977. Market shares are the primary indicia of market power, *United States* v. *Continental Can Co., supra,* 378 U.S. at 458. However, a further examination of the structure, history and probable future of the applicable market is necessary. *Jim Walter Corp., supra,* 3 CCH TRR at p. 21,316. (RPF 132.)

In *General Dynamics* as the Commission noted in *Jim Walter Corp., supra,* 3 CCH TRR at 21,317, "after a further examination of the 'structure, history and probable future' of the coal industry the Court concluded that [53] despite high levels of concentration in the industry other factors justified the conclusion that the acquisition would not have the requisite anticompetitive effect." (RPF p. 132.)

In *U.S.* v. *General Dynamics,* 415 U.S. 486 at 498 (1974), the Supreme Court upheld a district court's finding that, despite statistical market shares which appeared to show a concentrated market and an increased market share resulting from the acquisition, "other pertinent factors" affecting the industry and the business of the parties led to the conclusion that no substantial lessening of competition had occurred or was threatened by the acquisition.

There the evidence showed that: (a) coal was sold principally pursuant to long-term contract; (b) a producer's ability to compete in the future turned on whether or not it had the necessary reserves to negotiate new contracts; (c) although the acquired firm was financially healthy, by the time of suit its uncommitted reserves of recoverable coal were very low, and it was not in a position to increase them; and (d) as a result, the acquired firm could not compete effectively for long-term contracts and, accordingly, was "a far less significant factor in the coal market than the Government contended or the production statistics seemed to indicate." 415 U.S., at 499–504. "Irrespective of the company's size when viewed as a producer, its weakness as a competitor was properly analyzed by the District Court and fully substantiated that court's conclusion that its acquisition by Material Service would not 'substantially . . . lessen competition.' " 415 U.S., at 503–04.

The Court accepted the lower court's holding that there is a defense other than that the acquiree was failing to a charge that Clayton Section 7 has been violated.

Pillsbury's Failing Company Defense

One defense to a charge that Section 7 has been violated stems from language in *International Shoe Co.* v. *FTC,* 280 U.S. 291, 301–303 (1930). There the Supreme Court said:

> It is perfectly plain from all the evidence that the controlling purpose of the International in making the purchase in question was to secure additional factories, which it could not itself build with sufficient speed to meet the pressing requirements of its business.
>
> * * * * * * *
>
> [54] Shortly stated, the evidence establishes the case of a corporation in failing circumstances, the recovery of which to a normal condition was to say the least, in gravest doubt, selling its capital to the only available purchaser in order to avoid what its officers fairly concluded was a more disastrous fate. It was suggested by the court below, and also here in argument, that instead of an outright sale, any one of several alternatives might have been adopted which would have saved the property and preserved competition; but, as it seems to us, all of these may be dismissed as lying wholly, within the realm of speculation.
>
> * * * * * * *
>
> In the light of the case thus disclosed of a corporation with resources so depleted and the prospect of rehabilitation so remote that it faced the grave probability of a business failure with resulting loss to its stockholders and injury to the communities where its plants were operated, we hold that the purchase of its capital stock by a competitor (there being no other prospective purchaser), not with a purpose to lessen competition, but to facilitate the accumulated business of the purchaser and with the effect of mitigating seriously injurious consequences otherwise probable, is not in contemplation of law prejudicial to the public and does not substantially lessen competition or restrain commerce within the intent of the Clayton Act. To regard such a transaction as a violation of law as this Court suggested in *United States* v. *U.S. Steel Corp.,* 251 U.S. 417, 446–447, would "seem a distempered view of purchase and result." See also *American Press Ass'n* v. *United States,* 245 Fed. 91, 93–94.

[55] At that time Section 7 applied to lessenings of competition between the acquiring and acquired corporations. The Section was amended in 1950 to apply to lessenings of *competition* in any line of commerce.

Both houses of the Congress sanctioned the defense when Section 7 was amended in 1950 (H. Rep. No. 1191, 81st Cong., 1st Sess., 6 (1949): S. Rep. No. 1775, 81st Cong. 2d Sess., 7 (1950) as follows:

Companies in a failing or bankrupt condition

* * * * * * *

[T]he [Supreme] Court has held . . . that a company does not have to be actually in a state of bankruptcy to be exempt from its [Section 7's] provisions; it is sufficient that it is heading in that direction with the probability that bankruptcy will ensue.

* * * * * * *

It is expected that, in the administration of the act, full consideration will be given to all matters bearing upon the maintenance of competition, including the circumstances giving rise to the acquisition.

The "Report of the Attorney General's National Committee to Study the Antitrust Laws" (1955) also notes the existence of the failing company defense by reference to both *International Shoe* and the Congressional reports cited above (p. 123).

The requirements for establishing the defense were refined in *Citizen Publishing Co.* v. *United States,* 394 U.S. 131 (1969). There in holding that the defense had not been established the Court said that it had no occasion to determine what changes, if any, the 1950 amendment had on the failing company doctrine (n.3 at 137). The facts were that two newspapers — the Tucson Arizona Citizen and the Star — combined their business operations while maintaining separate news and editorial departments. The Court said that the ostensibly failing, merged corporation was not on the [56] verge of going out of business, that there was no serious probability that it would terminate its business and liquidate its assets unless the merger ("the last straw") was effected, that attempts to sell the firm never had been made and that the "failing" newspaper continued to be a significant threat "to the Star" (394 U.S. at 137). The Court added that the prospect of reorganization under Chapter XI of the bankruptcy Act ". . . would have had to be dim or nonexistent to make the failing company defense applicable. . ." (at 138) and that "We confine the failing company doctrine to its present narrow scope" (at 139).

Most recently — in an opinion dated February 22, 1978 — the Commission commented on the "failing company" defense when it adopted the initial decision of Administrative Law Judge (ALJ) Morton Needelman in *Reichhold Chemicals, Inc.*, Dkt. 9076 (July 19, 1977) [*supra*]. There the ALJ found that the "failing company" criteria had not been shown because Reichhold *met none of the* *requirements.* (n.92, p. 72, Initial Decision, slip copy). The defense was based on the fact that the acquired firm was weak and that *Reichhold discarded the acquired company* because it failed" . . . to come up to *Reichhold's* intra-corporate standards for profitability and efficiency" (p. 72, Initial Decision, slip copy). There is much evidence in this case as to Fox's poor financial condition and there is no evidence that Pillsbury intends to discard Fox. If there was, my attitude toward the acquisition would be much different.

The Reichhold decision continued:

> There is no such quasi-failing company defense available under Section 7 of the Clayton Act. The market is supposed to determine whether firms fail or not, and the very purpose of the "failing company" doctrine is to preserve (and not discard as Reichhold did) an entity which would have collapsed but for the acquisition. *International Shoe Co.* v. *FTC,* 280 U.S. 291 (1930). As for the use by a large firm of *its* internal standards to determine whether a [57] small competitor fails or not, the legislative history of Section 7 indicates that the Congressional intent was just the opposite — Congress wanted to stop acquisitions which give large firms discretionary power over the continued development or, for that matter, the existence of their smaller competitors. *Crown Zellerbach Corp.* v. *FTC,* 296 F.2d 800 (9th Cir. 1961), *cert. denied,* 370 U.S. 937; see also concurring opinion of Mr. Justice Douglas in *United States* v. *Falstaff Brewing Corp.,* 410 U.S. 526, 538 (1973). At 72.

Counsel for Pillsbury then has not made out the failing company defense. Fox had not yet reached the extreme financial distress situation which these decisions suggest must be present for the defense, in and of itself, to insulate the acquisition from being found to be a violation of Section 7. But its precarious position when considered in the light of other factors convinces me that the acquisition did not violate Clayton Section 7, or consequentially FTCA Section 5.

Pillsbury's No-Public-Interest Defense

Counsel for Pillsbury contends that this proceeding is not in the public interest (RB, pp. 46–50). This is because, in summary, Fox's plant was not operated in accord with U.S.D.A. and other federal regulations affecting health and safety and Pillsbury was able to and did correct the deficiencies.

These points raised by counsel for Pillsbury do have a bearing on the "General Dynamics" defense discussed below because they address the question of whether Fox indeed was or probably would be able to have an impact on competition in the frozen prepared pizza industry.

Insofar as the points are intended to address a no-public-interest defense, however, the Commission has said that question is reserved to itself and that it is not to be ruled upon by the administrative law judge. In [58] deciding to issue a complaint, the Commission proper, in accord with Section 5(b) of the FTC Act, determines that it has "reason to believe" that the proceeding is "to the interest of the public." Two holdings by the Commission to this effect are *Exxon Corp.*, 83 F.T.C. 1759 (1974) and *Herbert R. Gibson, Sr., et al.*, Dkt. 9016, October 12, 1977.

Lastly, respondents conceded that entry of the court's order was in the public interest when it entered into a stipulation with Commission attorneys in connection with settlement of the Commission's suit for a preliminary injunction. (See p. 3 above.) If entry of the order after the preliminary injunction to stop the acquisition of Fox by Pillsbury and agreeing to the terms of the preliminary injunction issued are in the public interest, it follows that these administrative proceedings are "to the interest of the public"—the language of FTCA Section 5. [59]

The General Dynamics Defense

An appellate court decision on November 4, 1977, in *United States* v. *International Harvester Company,* 564 F.2d 769 (7th Cir. 1977) upheld a district court opinion (U.S.D.C., No. Dist. of Illinois, Eastern Division — the same court which issued the preliminary injunction in this case — see p. 2, above) in which the "General Dynamics" defense 415 U.S. 486 (1974) was established. The circuit court said (564 F.2d at 773) that evidence of the acquired firm's "weakness as a competitor" properly was considered by the district court as rebuttal to the government's statistical evidence which had established that the acquisition was presumptively illegal. See *Marine Bancorporation, supra,* 418 U.S. at 631.

Even accepting the statistics as the primary index of market power "only a further examination of the particular market — its structure, history and probable future — can provide the appropriate setting for judging the probable anticompetitive effect of the merger." *Brown Shoe,* 370 U.S. at 322, n.38, quoted in *General Dynamics,* 415 U.S. at 498.

The evidence in *International Harvester* showed that even if the acquired firm had remained in the market ". . .it did not have sufficient resources to compete effectively, and this supports the district court's conclusion that the acquisition of 39 percent of Steiger's stock by Harvester would not substantially lessen competition. See [*General Dynamics*] 415 U.S. at 508, 509-510, 94 S. Ct. 1186." 564 F.2d at 774.

The evidence here shows that Fox in an intensely competitive industry dominated by large firms, was financially weak, had production problems requiring capital for investment Fox did not have, could not offer advertising assistance or other promotions which successful competition in the frozen prepared pizza industry demands and had a division which even complaint counsel's witness said was debilitating Fox and on the sale of which the witness' testimony as to Fox's viability hinged. (Findings 110–113; 15–17, 19–27, 30–32.)

Footnote 7 (564 F.2d 773) of the *International Harvester* opinion elaborates on the thinking of the circuit court:

Although the Government asserts that *General Dynamics* is distinguishable on the facts (Br. 22 n.20, Reply Br. 11 n.9), the rationale of that **[60]** case was not limited to situations involving limited amounts of a natural resource, such as the coal reserves at issue there. On the contrary, in a rapidly expanding industry in which plant expansion and an ability to keep pace with demand are as Judge Leighton concluded, "needed * * * to take advantage of the growing * * * market" (finding 33), current sales and production, taken apart from the availability of capital, are no less "unreliable indicators of actual market behavior," *United States* v. *Marine Bancorporation, supra,* at 631, 94 S. Ct. at 2875, than production was in *General Dynamics* when taken apart from coal reserves. Moreover, the type of evidence that the Supreme Court itself has considered after *General Dynamics* (see *United States* v. *Citizens & Southern National Bank, supra,* at 121, 95 S. Ct. 2099; *United States* v. *Marine Bancorporation, supra,* at 631–632, 94 S. Ct. at 2874–2875) indicates that the "*General Dynamics* defense" is not to be limited to the absence of resources, either natural or monetary, but rather should include, at least as the Government admits elsewhere in its brief, those "special circumstances" in the case that indicate that the "statistical data did not provide a reliable indication of the future effect of the acquisition" (Br. 19 n.18), or perhaps even more broadly, any evidence indicating that statistical projections may be unreliable, *cf. United States* v. *Amax, supra,* 402 F. Supp. at 970.

As indicated above (Findings 14–17, 19–32; 35), the Pillsbury-Fox situation is analogous in a sufficient number of ways to convince me that the *International Harvester* decision is precedential to this case. **[61]**

To the same result are a number of Commission decisions in response to requests for advisory opinions. These indicate that an acquisition was approved when it apparently was improbable that substantial, adverse effects on competition would ensue:

> (1) A large diversified manufacturer was granted clearance to acquire the second largest integrated manufacturer of a specialty closure product. The top four firms accounted for 55% of the market and the acquiree was in poor financial condition. Advisory Opinion Digest 169; 1 CCH TRR ¶ 4295.98.
>
> (2) Clearance was granted to acquire a deteriorating competitor doing business in a limited geographical area by a firm

operating nationally after reasonable but unsuccessful efforts had been made to find another buyer. Advisory Opinion Digest 165; 1 CCH TRR ¶ 4295.07.

(3) Two large food processors subject to an order requiring prior approval were permitted to acquire a small food processor which had declining profits, too small a plant and the owner was determined to sell. Advisory Opinion Digest 185; 1 CCH TRR ¶ 4295.17.

Also see Advisory Opinion Digests 177 and 179; 1 CCH TRR ¶ 4295.35, "Equities." **[62]**

The Section 5(a)(1) Charges in the Complaint

As noted in the beginning of this initial decision (p. 1) the complaint alleged that both Clayton Section 7 and FTCA Section 5 were violated by Pillsbury and Fox by (1) consummation of the acquisition and (2) by having contracted to make the acquisition. Since these allegations hinge on the Section 7 aspects and have not been separately addressed by argument or evidence offered there is no basis for finding that FTCA Section 5 was violated as alleged.

Respondents Request for Attorneys Fees and Costs

With regard to respondent Pillsbury's request for attorneys fees and costs (p. 4) above; Answer, last par., p. 5) there is no provision in the Commission's adjudicative (Part 3) rules for such payments. There is a provision in Part 1, Section 1.17 "Compensation for representation in rulemaking proceedings," that is grounded on inability of a person having a legitimate interest in the trade regulation rule proceedings to participate ". . .because such person cannot afford to pay costs. . ." (subparagraph (a) of Section 1.17). Clearly, the provision does not apply to adjudicative proceedings or to a respondent such as Pillsbury. *See also,* "Magnuson-Moss Warranty—Federal Trade Commission Improvement Act," 15 U.S.C. 2310(a)(5)(d)(2).

Conclusions

1. The Commission has jurisdiction of and over the respondents, the subject of this proceeding and the proceedings were and are to the interest of the public.
2. Pillsbury was and is a corporation engaged in commerce, as "commerce" is defined in the Clayton Act.

3. Fox was a corporation engaged in commerce, as "commerce" is defined in the Clayton Act, when it was acquired by Pillsbury.

4. The appropriate line of commerce — product market — to be considered in judging the legality of the acquisition of Fox by Pillsbury is frozen prepared pizza.

5. The appropriate section of the country — geographic market — in which the competitive effects of the acquisition are to be examined is the United States as a whole. [63]

6. The effects of the acquisition of Fox by Pillsbury were, or probably will be, that:

(a) Fox was eliminated as a competitor in the frozen prepared pizza industry;

(b) Concentration in the frozen prepared pizza market has been increased because one competitive entity has been combined with another;

(c) The competitive position of Pillsbury vis-a-vis its competitors in the frozen prepared pizza has been improved; and

(d) enhancement of Pillsbury's competitive vigor probably will result in a substantial increase in competition in various sections of the country in which Pillsbury did not compete previously in the frozen prepared pizza industry.

7. Fox was not a "failing company" in the sense in which that term is used in connection with Section 7 but the evidence as to its precarious financial condition coupled with the insignificance of the competition it offered and was likely to offer in the frozen prepared pizza industry rebuts the prima facie proof of violation which complaint counsel's presentation established.

8. The complaint should be, and hereby is, dismissed.

Dissenting Opinion of Commissioner Dixon

I agree entirely with the first six sections of the Commission's opinion but I cannot join its conclusion that this merger is unlikely substantially to lessen competition in the national market for frozen prepared pizza.

The merger combined firms with approximately 15% and 2% of the national market.[1] This occurred in an industry in which concentration has been increasing at an alarming rate. In the three

[1] Several sets of market share figures were cited by the ALJ. Those that appear most reliable were prepared by Selling Areas Marketing, Inc., (SAMI), I.D. 78-99, and will be cited herein. Pillsbury's market share in 1976 was 15.4% and Fox's was 1.7% Fox's share of the market had declined from 2.4% in 1975. This may have been due in significant part to its move to new production facilities in Joplin, Missouri, in which it encountered start-up problems and was only producing at 50-80% of capacity in March, 1976. (CX 49) Thus, I believe that "approximately 2%" is a reasonable characterization of its market share, and I certainly see no warrant for

(Continued)

years preceding the merger, the top three firms increased their market shares from 39.65% to 53.37%, while [2] 7-firm concentration rose 10 points from 70.74% to 80.74%. (I.D. 106) Respondent's Vice President of Mergers and Acquisitions projected that the top three companies will capture 60–70% of the national market by 1980. (Tr. 175)

As the Supreme Court has told us, it is the basic premise of Section 7 of the Clayton Act that competition will be most vital "when there are many sellers, none of which has any significant market share." *United States* v. *Philadelphia National Bank,* 374 U.S. 321, 363 (1963). It may well be that in the market we deal with here, preservation of many small sellers, or even prevention of a tight oligopoly, is impossible, but I think that it is the purpose of the antitrust laws to ensure that at least the attempt is made.

While Fox's competitive vigor may well not have been on the order of that displayed by those companies of even smaller market share whose acquisition was condemned in *United States* v. *Aluminum Co. of America,* 377 U.S. 271 (1964) and *Stanley Works* v. *FTC,* 469 F.2d 498 (2d Cir. 1972), *cert. denied,* 412 U.S. 928 (1973), neither can I conclude that Fox was quite the competitive cipher that the majority describes. For many years Fox was a thriving, growing vendor of frozen pizza, with sales concentrated in a number of metropolitan areas in the Midwest and South. (I.D. 133–34) The company never failed to realize a profit, and as late as the September preceding its November acquisition it showed earnings of $43,000. In the year prior to the merger, Fox sold over $7 million worth of pizza, which gave it 2.4% of the national market. In 1976 it moved to different quarters, a non-recurring factor that may have contributed to its decline in market share to 1.7%. But neither the 1975 nor 1976 figures for the *national* market adequately account for Fox's competitive significance, because Fox's sales were limited to only certain areas of the country, in some of which it was in head to head competition with Pillsbury.[2] [3] The record is clear that in those areas of the country in which Fox did compete, it sold to such leading

characterizing Fox's share as a "declining 1.7%" when the decline *to* 1.7% may very possibly have been due in significant measure to non-recurring factors.

[2] Fox made 44% of its retail sales of frozen prepared pizza, exclusive of private label sales, in only nine metropolitan areas in the South and Midwest, during 1975–76, and Pillsbury made 25% of its total sales in those same areas during the same period. These nine areas accounted for only 16% of national pizza consumption. Fox's share in those areas ranged from 2% to more than 16% in 1975. (CX 36 *in camera*)

I agree with the Commission's finding of a national market, and with its conclusion that the record generated in this case will not support delineation of any particular regional submarket. However, not all pizza manufacturers sell in all marketing areas, nor would it be realistic for many to do so. For example, even an industry leader like Pillsbury has not entered the trade areas of New England, New York, and Los Angeles, due to insufficient production capacity. (I.D. 130) Retailers in these trade areas, then, could not realistically turn to Pillsbury in the event that they perceived wholesale prices to be getting out of line, unless perhaps prices became so distorted that Pillsbury was willing to reorient its marketing efforts. The situation with smaller producers is

(Continued)

retail food chains as Kroger and Winn-Dixie, and was regarded by leading frozen pizza producers as a "substantial competitor." (I.D. 109)

Under these circumstances, in a highly concentrated market hell-bent toward further concentration, I believe that the antitrust laws should be read to preclude the combination of one of the industry's leading firms with one of its smaller but nevertheless "substantial" competitors. As the Second Circuit Court of Appeals noted in *Stanley Works* v. *FTC, supra,* involving the joinder of an industry leader with a firm with 1% of a market in which 4-firm concentration was 49–51% (vs. roughly 60% here) and there was no comparable record evidence of increasing concentration:

> . . . though a market may be concentrated, forces may operate so as to maintain some level of competition and thus preserve the possibility of eventual deconcentration. That is why the continued independence of companies with relatively small market shares is so crucial to the health and vitality of a market threatening to become oligopolistic. 468 F.2d at 508.

Of course, one does not know how long Fox might have stood alone, but if precluded from selling out to an industry [4] leader, we may surmise that it would have combined either with a smaller industry member, or sold out to an outsider seeking to enter, either of which results would have been competitively preferable to the one that actually occurred.

The Commission, mindful of these considerations, finds that "there is no reason to believe that Fox, if acquired by a company outside the market, could have constituted a springboard to permit a new entrant to challenge the market leaders," and further, that barriers to entry were so low anyway that a potential entrant might do just as well by attempting *de novo* entry as by acquiring Fox. I find both these assertions to be unproven on the record, and I believe that it is respondent's burden to prove them if it wishes to consummate a horizontal merger of more than *de minimis* proportions in an industry as highly concentrated and with so pronounced a trend toward concentration as this one.[3]

even more pronounced in this respect. For these reasons I believe that it is proper to qualify the national market figures with some consideration of local marketing areas in which the merging parties competed, and doing so leads to the conclusion that the national figures understate the overall significance of this merger.

[3] This is also the position of the Department of Justice Merger Guidelines, of which this merger is in plain violation. Guideline 7 provides that the Department will ordinarily challenge a merger in any market, "not wholly unconcentrated" (which certainly characterizes 4-firm concentration of 60%) in which the aggregate market share of any grouping of the two to eight largest firms has risen by 7% or more during a five to ten year period preceding the merger (here 3-firm concentration rose by 13% in only *3* years), and which involves the acquisition by any firm in the relevant grouping of two to eight firms of any other firm whose market shares amounts to "approximately 2% or more." 1 Trade Reg. Rep. ¶4510 at 6884 (1971). I have earlier explained why I believe that "approximately 2%" is an abundantly fair characterization of Fox's market share. In all other respects, the characteristics of this industry far exceed those required to trigger prosecutorial action by the Department of Justice.

While one witness did testify that he had entered on the local level with an investment of only $50,000, it is plain from the record that entry on a nationwide or regional basis is a considerably harder proposition, and is becoming ever more so. In addition to capital costs (examples of which were $15 million to build a new plant for Pillsbury, down to $3 million paid by Purex to lease and improve its facility, I.D. 147) the ALJ found that considerable advertising and promotional expenditures are required to gain distribution of frozen prepared pizza, and a company must be prepared to sustain losses over an extended interval before effecting successful entry. (I.D. 148–50) While Fox was not a heavily advertised name brand, it obviously did have [5] considerable retailer recognition and entree into many important local marketing areas. For these reasons, I cannot conclude that Fox's assets would have proven altogether unattractive (or of no advantage over *de novo* entry) to a well-endowed potential entrant in search of a means of entering the frozen prepared pizza market.[4]

Of course, my surmise may be wrong, as may be that of the majority. The question, however, is who should bear the burden of proof in a case such as this. In my view, where concentration is as high, and increasing as rapidly, as it is here, a horizontal acquisition of more than *de minimis* proportions by a leading industry member should be presumed unlawful unless shown to the contrary.[5]

The Commission decision appears to rest importantly upon the fact that, in absolute terms, Fox was a very small company. I agree that this is an important concern in two respects. First, the absolute size of a company may be probative of its potential competitive ability. Secondly, and this appears to be a consideration upon which the majority's opinion turns heavily, there may be a countervailing competitive value in facilitating the ability of small companies to sell out, because ease of exit is an encouragement to entry by small entrepreneurs, and that is a competitive good. I share these concerns, but the problem is how to balance a global competitive consideration such as "encouraging entry by small entrepreneurs"

[4] I also find it interesting that in an industry in which entry barriers are assertedly so low, concentration should be increasing so quickly. Low entry barriers imply low scale economies — *i.e.* a firm with only a small market share can sell profitably at the same price as a firm with a larger market share. Why, then, do smaller firms seem to be uniformly losing out to larger ones? One reason may be, as the Commission itself has previously recognized, that increased concentration and the necessity to do battle with deep-pocketed competitors, may themselves be formidable barriers to entering or remaining in an industry. Cf. *Fruehauf, Inc.*, 91 F.T.C. 132, 220 (1978), appeal pending.

[5] This merger is clearly not of *de minimis* proportions. In *Stanley Works* v. *FTC, supra*, the Second Circuit sustained a Commission finding that the loss as an independent competitor of a company with a 1% market share, consisting of less than $900,000 in sales yearly, constituted a substantial lessening of competition. 469 F.2d 498, 501 n.7.

against the potential loss of competition from the acquisition of one of these small entrepreneurs in a particular market. [6]

I certainly agree, as the Commission states, that it is desirable that "owners of very small businesses with slight competitive potential have some reasonable flexibility to sell out." (Op. p. 19) I even agree that owners of very small businesses with not insubstantial competitive potential, like Fox, should have some reasonable flexibility to sell out if they tire of the competitive whirl. I do not agree, however, that such "reasonable flexibility" must include an absolute right to sell to a leading horizontal competitor in a very concentrated industry in which concentration is increasing. At a minimum, the Commission should insist under such circumstances that reasonable good faith efforts be made by the very small competitor to sell to someone other than a leading industry member before sale to the industry leader is condoned. Here, of course, as the majority acknowledges, (Op., p. 10) we have no evidence that any such reasonable efforts were made. If such reasonable efforts are not required, then we may predict that very small competitors will invariably seek to sell to industry leaders, because it is they who are most likely to be willing to pay a premium for the ability to snuff out a pesky opponent and acquire its share of the market. In the industry involved here, the likelihood of this occurrence is a matter of record. The president of one leading firm testified that Pillsbury's acquisition of Fox inspired his firm to consider a similar acquisition of a small competitor (a peculiar reaction if Fox's competitive value is as slight as the Commission imagines) though consummation awaits disposition of these proceedings. (I.D. 108)

The Commission purports to read the *General Dynamics* and failing company defenses narrowly, but its holding in essence applies a more lenient version of these defenses to the case of a very small acquired firm. If liability is made to hinge upon proof (by which side we are not told) of (1) entry barriers; (2) whether a company lacks "any special competitive potential"; and (3) whether there is "reason to believe that the acquired company, in other hands, would have been a vehicle leading to less concentration or more competition," then I cannot see how proof under the Commission's new "line of legality" will differ from proof under the old lines drawn by the courts. I do not mean by this to imply criticism of the Commission's approach — I quarrel only with the implication that it will make life any easier, or less remunerative, for the antitrust bar. Cases on the borderline of illegality inevitably involve difficult judgments. I agree that very small companies should be treated gently when they seek to exit, and I agree that the factors [7] considered by the Commission

(Op. p. 21) are important ones. I would simply add, however, that if the purpose of favoring small company mergers is to facilitate exit and thereby encourage entry, we should insist before condoning such mergers where they might otherwise violate the antitrust laws that a demonstration be made that there have been reasonable, good faith efforts to sell to someone other than a leading horizontal competitor.

Fox Deluxe Foods ranked ninth in the frozen prepared pizza market when it was acquired. Under the Commission's rationale, it is not clear how we can possibly object if the top eight firms in this market should now proceed to divide among themselves all the rest, since the top eight firms already control 85.52% of the market (I.D. 105), and could absorb the other 14% by means of each acquiring the 2% to which the Commission's decision entitles it. Competition in the sale of frozen prepared pizzas may now be (as it usually is in the estimation of industry members) "tough". I daresay, however, that when, in a few years, the firms that remain in this industry wake up to find themselves facing only seven competitors nationwide and far fewer that that number in any given local marketing area, they will discover, with no offense to the antitrust laws, a far more lucrative way of pricing their pizza than they have utilized to date. Perhaps this occurrence cannot be prevented, but I had always thought that the Clayton Act was designed to allow the government to try. As I read the record before us I would find that the challenged merger violates the law.

Concurring Opinion of Chairman Pertschuk

I concur in the Commission's determination that the acquisition of Fox by Pillsbury does not violate Section 7 of the Clayton Act or Section 5 of the FTC Act. For the reasons enumerated in the Commission's opinion, relating to the size and market share of the acquired firm and its lack of any special competitive potential, the absence of significant entry barriers, and other factors, this merger is not likely to have significant anticompetitive effects in the national market for retail frozen prepared pizza. I wish only to add my view that the formulation of any general rule of broad application out of the particular set of facts in this case would be a difficult and speculative task indeed.

Further, while I agree that preserving exit opportunities for very small firms can be procompetitive insofar as it indirectly lessens entry barriers, I believe that this consideration will influence the ultimate determination of a horizontal merger's lawfulness in only a very limited set of circumstances. I do not read the Commission's opinion to hold otherwise.

Opinion of the Commission

By Pitofsky, *Commissioner:*

I. Introduction.

This is a merger case involving an acquisition by the Pillsbury Company ("Pillsbury"), a leading manufacturer and marketer of a wide range of food products, including frozen prepared pizza, of Fox Deluxe Foods, Inc. ("Fox"), a rather small company with assets devoted in large part to the production and sale of frozen pizza. As will emerge below, Pillsbury-Fox was clearly a horizontal merger and resolution of the question whether that merger is illegal raises important questions about the location of the "bottom line" beneath which even horizontal mergers will be found not to violate Section 7. At issue are interrelated policy questions involving the "failing company" defense, the increasingly popular *"General Dynamics"* defense, and the definition of insubstantial anticompetitive effects under Section 7.

The complaint issued in this case in November 1976 charging that the merger between Pillsbury and Fox would substantially lessen competition in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. 18, and Section 5(a)(1) of the Federal Trade Commission Act, 15 U.S.C. 45. On November 15, 1976, the respondents stipulated to a [2] Preliminary Injunction which permitted the merger to be consummated, subject to certain conditions.[1]

The administrative law judge ("ALJ") dismissed the complaint. He found that a relevant market in which to assess the effects of this transaction was the retail sale of frozen prepared pizza in the United States. He further found, based on statistics prepared by Selling Areas Marketing, Inc. ("SAMI"), the four-firm concentration in the relevant market to be 60.8%, and that in 1976, the year of the acquisition, Pillsbury ranked third in the national retail frozen prepared pizza industry with 15.4% of sales, and Fox ranked eleventh with 1.7% of sales. (I.D. 104, 105)[2]

After finding that Pillsbury and Fox were horizontal competitors, the ALJ went on to reject the "failing company" defense proffered by respondents and deferred ruling on their contention that the proceeding was not in the public interest, stating that "the Commis-

[1] The complaint was amended to reflect the fact that the acquisition had been completed.

[2] The following abbreviations are used herein:

I.D.	- Initial Decision Finding No.
I.D. p.	- Initial Decision Page No.
CX	- Complaint Counsel Exhibit No.
RX	- Respondent Exhibit No.
Tr.	- Trial Transcript Page No.

sion has said that question is reserved to itself." (I.D. p. 57) Nevertheless, the ALJ relied upon Fox's "precarious position" (I.D. p. 57) as establishing a *"General Dynamics"* defense — that is, a defense based in his view, on the opinion in *U.S.* v. *General Dynamics,* 415 U.S. 486 (1973), in combination with *U.S.* v. *International Harvester Company,* 564 F.2d 769 (7th Cir. 1977). The ALJ dismissed the complaint, noting the following:

> Fox was not a "failing company" in the sense in which that term is used in connection with Section 7 but the evidence as to its precarious financial condition coupled with the insignificance of the competition it offered and was likely to offer in the frozen prepared pizza industry rebuts the prima facie proof of violation which complaint counsel's presentation established. (I.D. p. 63)

We affirm the dismissal of the complaint but on significantly different grounds. Our own review of the issues follows: [3]

II. The Industry.

There is general agreement among the parties, and the record supports the view, that the retail frozen prepared pizza industry has been undergoing substantial change. While most present manufacturers began as very small operations, often originating with a small pizzeria, brands are now developed for immediate nationwide distribution. Sales of frozen pizza grew from $407 million in 1975 to $463 million in 1976. (I.D. 102) Spurred largely by the recent entry — both by acquisition and by internal expansion — of national firms of substantial size,[3] the focus of competitive activity has shifted into intensive advertising and promotion.

Small manufacturers nevertheless remain viable. Market leaders differ regionally and locally, and private labelling has increased. Given the cost of plant, equipment, and the necessary advertising and promotional expenditures, it could take several million dollars to enter the retail frozen prepared pizza market on a nationwide scale. On the other hand, one pizza manufacturer testified that it was possible to enter the business on a local scale with a total investment of only about $50,000. (I.D. 151)

III. The Merging Parties: Pillsbury and Fox.

Pillsbury manufactures and markets a wide range of food products and is among the 200 largest U.S. corporations. (I.D. 4, 5) It entered the frozen prepared pizza business by its November, 1975 acquisition

[3] Pillsbury itself entered the industry by acquiring Totino's in 1975. General Mills acquired Saluto's in 1976, Purex acquired Ellio's in 1971, and Quaker Oats entered through its 1969 acquisition of Celeste. Large companies that entered *de novo* by developing their own product include Pet, Inc. Ore-Ida (Heinz), Fairmont Foods, and Stouffers. (I.D. 114).

of Totino's Finer Foods, Inc. Totino's gross sales of frozen prepared pizza for the twelve months ending October 31, 1975 were approximately $39 million (I.D. 6), and it ranked third in the industry with 13.7% of national sales. (I.D. 100)

Prior to its acquisition by Pillsbury, Fox was a family-owned Illinois corporation headquartered in Chicago. Until 1975, it was a profitable enterprise. Its sales increased from $6.4 million in 1972 to $11.2 million in 1975; over the same period its net worth increased 50%. (I.D. 18) However, one of Fox's two operating divisions, the Hotel and Restaurant ("H&R") Division, after showing profits through 1972, ran losses each year thereafter. The H&R Division was in the business of processing and selling various food products — primarily poultry — to food service customers such as [4] hotels, fast-food carryouts, hospitals, restaurants and the like. In February 1975, Fox's Board of Directors determined that a final decision on the fate of the H&R Division had to be made within six months. (CX 47)

Fox's Country Kitchen Division made and sold frozen prepared pizza, and was responsible for Fox's overall profitability through 1975. Fox's pizza sales in 1974 increased 20% over its 1973 sales. (CX 47) Although in 1975 Fox had freezer problems at its pizza plant in Carthage, Missouri, which necessitated the once-only expenditure of $350,000 over the course of approximately twelve months (Tr. 2409), and despite an unusually warm autumn that year which adversely affected frozen pizza sales (I.D. 30), Fox's pizza division remained profitable through 1975.

The Fox-produced frozen pizza had some reputation in the industry as a "price" or "in-and-out" brand (Tr. 1063), selling on the strength of low prices and numerous discount promotions. Fox did not engage in extensive advertising. (I.D. 11)

Although Fox took no effective action to initiate acquisition discussions, it was approached during 1975 by two companies to discuss a possible acquisition. The Peavey Company initiated contact with Fox, on the recommendation of a merger consultant. (Tr. 2595) Fox ultimately was not considered a suitable target for Peavey since Fox's line was positioned in the low-price, low-quality segment of the market, which made it incompatible with Peavey's other products. (I.D. 16) Peavey also doubted Fox's management strength and, based on a description of what was to be Fox's new plant, doubted that it "would be a plum." (Tr. 2600)

Early in January, Joe Fox met with a Vice-President of the Anderson-Clayton Company, a Houston-based food and food-related producer and distributor. (I.D. 17) The meeting was set up in response to a letter from Anderson-Clayton inquiring about Fox's interest in being purchased. (Tr. 2855) No follow-up visit or visit to Fox's Carthage plant was ever arranged.

At the end of 1975, Fox's Board of Directors decided to move its pizza operation from Carthage to a new plant in Joplin, Missouri. Fox applied to the Harris Trust and Savings Bank ("Harris"), with whom the company had banked since 1953, for a loan to finance the move. A $300,000 unsecured revolving loan — a line of credit — was approved. Harris had witnessed a "dramatic turnaround" in Fox's fortunes from 1972 to 1975, due to the success of the pizza division. (RX 48) Consequently, the short-term line of credit was extended despite its intended use to finance long-term [5] assets, on the assumption that it could be paid off easily with the proceeds of the anticipated liquidation of the H&R Division. (I.D. 18) Negotiations with Bon Ton Poultry Products, Inc. ("Bon Ton") for the sale of that Division were underway at the time.

Fox encountered a series of business misfortunes and adversities in 1976, but they were never so severe as to turn its pizza division into a failing operation. Fox's move to Joplin at the beginning of the year encountered start-up troubles. By March, production was only 50 to 80 percent of capacity (CX 49), and some of the equipment, much of which had been moved from Carthage, was causing problems. (I.D. 24) Nevertheless, Fox's Board of Directors was told that the quality of the product was "greatly improved in the Joplin plant" and production costs "were already lower". (CX 49) In light of the start-up problems and delays in the sale of Fox's H&R Division, Harris extended the outstanding line of credit for ninety days.

Things got no better as the year progressed. Sales were running twenty percent below projections, most of the losses due to increases in "controllable costs" (RX 16) which, unfortunately, were not being controlled. In May, Harris approved a temporary $50,000 "excess" to tide Fox over, due and payable at the end of June with the $300,000 already outstanding. (I.D. 22) The H&R Division continued to generate losses, draining needed capital from the pizza division. (RX 16) It was about this time, with its business prospects gloomy and other prospective buyers out of the picture, that Fox was first made aware of Pillsbury's interest in acquiring Fox's pizza manufacturing assets.

In June, the new Joplin plant was given a "4", the highest rating by inspectors from the U.S. Department of Agriculture. While problems remained,[4] Fox had agreed to take curative measures, and

[4] The plant was never wholly rodent-proofed, the meat room floor was deteriorating, the cooker leaked, the oven was hard to clean and caused fires of pizza crusts, and there was peeling paint in the sauce and meat rooms. (I.D. 15)

in any event the problems had "never caused an unsanitary, unwholesome or adulterated product to be produced at the Joplin facility." (CX 76) Estimates of the amount of investment required to bring the Joplin plant into full and non-temporary compliance with U.S.D.A. requirements varied, but none predicted that the [6] necessary amounts would be beyond Fox's current financial capacity.[5] Shortly thereafter, Harris increased Fox's unsecured line of credit from $350,000 to $500,000 for an additional ninety days, by the end of which time it was understood that either the H&R Division would be sold, all of Fox would be sold, or Harris would secure its loan and set up a repayment program. (I.D. 25) On July 22, 1976, Pillsbury's Vice-President of Mergers and Acquisitions, made a verbal offer to purchase Fox. (CX 46–23; CX 51)

At the Board of Directors meeting in August, Joe Fox reported on Pillsbury's offer of approximately fourteen dollars worth of restricted Pillsbury common stock for each outstanding Fox share. The Board rejected the offer as insufficient, but remained interested. The Board also voted to reject, without continued interest, the latest offer by Bon Ton for Fox's H&R Division.[6] (CX 51)

The pizza operation showed a profit in September, 1976 of $43,000. (CX 67) The H&R Division had not been sold, and an influx of capital was still needed to bring the Joplin plant to top efficiency. A memo from Fox's Vice President for Operations to its President outlined $280,000 worth of items which would be necessary if the Joplin plant were to meet all government requirements, provide product safety, improve case costs, provide employee safety, maintain the current level of performance, and improve the quality of the product. (RX 15)

The pizza division of Fox remained profitable throughout the fall of 1976. According to Mr. Horsch, president of a venture capital firm who testified as an expert witness on behalf of Pillsbury, "[t]he average profitability [of the pizza division] in the three months prior to the acquisition, which were the significant profitable months, was about thirty thousand dollars a month." (Tr. 2721)

Pillsbury acquired Fox on or about November 15, 1976, paying $3 million in Pillsbury common stock. On the same day it acquired Fox, Pillsbury sold the H&R Division to Bon Ton, for $174,500 in cash and $80,183 in notes. (CX 74) Pillsbury had also acquired the H&R Division's $365,000 worth of accounts receivable, and collected

[5] The Fox Board of Directors voted on June 14, 1976 to spend $61,820 to upgrade the plant. (CX 50) A June 3, 1976 memo to the Chairman of the Board from Fox's President Boyce, and Vice President of Operations, Balster, had estimated that only $36,000 would be necessary to solve all the problems noted by the U.S.D.A. inspectors. (Tr. 2408)

[6] At issue was the manner by which the H&R Division's accounts receivable could be collected. (I.D. 27) Fox wanted Bon Ton to take steps culminating in the placement of customers on a C.O.D. basis at Fox's direction if they failed to pay within a stated time. Bon Ton refused. The Fox Board voted to terminate the negotiations.

$307,000 against those receivables within a few months. (Tr. 2889) Pillsbury also turned out to have acquired $272,000 worth of signed but unmailed checks to various suppliers of both divisions of Fox, for the payment of which Pillsbury advanced $130,000. (Tr. 2888) Taking their assets and debts into account, the total acquisition price was approximately $3,156,000.

IV. Relevant Markets.

The parties agree that the United States is a relevant section of the country. Complaint counsel also suggest — and respondents dispute — that there are various regions, which correspond more or less to the greater metropolitan areas SAMI uses as bases for its statistics, which also constitute relevant geographic submarkets for the assessment of the effects of this merger.

There is considerable evidence that retail frozen pizza manufacturers often target, or even confine, their marketing regionally. Thus, in any particular city, only Pillsbury, Fox, and three or four other frozen pizza manufacturers might be selling at any given time. In such local markets Pillsbury's and Fox's market shares of course would be high and perhaps sufficient to indicate anticompetitive effects under Section 7. But "[w]e do not believe the pie will slice so thinly," *Tampa Electric Co.* v. *Nashville Coal Co.*, 365 U.S. 320, 331 (1961), at least not on this record. The test for measuring geographic market is where consumers (in this case retailers) can practicably turn for an alternative source of supply. *Tampa Electric Co., supra,* 365 U.S. at 327; *U.S.* v. *Grinnell Corp.*, 384 U.S. 563, 588 (1966) (Fortas, J., dissenting). *See also U.S.* v. *Philadelphia National Bank,* 374 U.S. 321, 357–9 (1963). Here the record is clear that frozen pizza manufacturers could sell virtually throughout the United States from a single plant with no significant cost disadvantages.[7] (I.D. 125–128, 131) Thus, the power [8] of any given group of sellers serving a city or region at a given time to raise price is limited by the capacity of virtually all other domestic manufacturers to compete on practically an equal footing in that city or region — an economic situation which requires a finding of a national market and the elimination of geographic submarkets.[8]

Respondent contests the ALJ's finding that retail frozen prepared pizza is a relevant product market, arguing that the market is too narrowly defined. Respondent contends, first, that all forms of pizza

[7] The fact that transportation costs pose no significant barriers to distribution to remote customers is evidenced by the finding that "[e]ven a small manufacturer like 'Tree Tavern' " from New Jersey can ship to Puerto Rico and the U.S. Virgin Islands. (I.D. 125)

[8] Even under these circumstances, of course, special factors, like slight economic barriers, could produce submarkets. However, the record in this case contains no evidence on which to base such findings.

— including dry mix pizza, refrigerated pizza, grocery shelf-stable pizza, restaurant pizza, and pizzeria pizza — must be included in the market, basically because "they are functionally interchangeable for the purpose for which they are made." (Respondent's Answering Brief, p. 31) Other frozen foods are also claimed to be effectively competitive, since frozen prepared pizza must vie with those products for space in the grocer's freezer chest. We think respondent describes an unduly wide competitive arena.

To find his way along the imprecise route toward product market definition, the ALJ turned to the familiar guideposts of *Brown Shoe Co.* v. *U.S.,* 370 U.S. 294 (1962). He found that retail frozen prepared pizza exhibited a number of characteristics, sufficient to identify it as a separate line of commerce (I.D. p. 43): unique characteristics of pizza preparation (the use of preservatives and blastfreezing); the fact that those companies which manufacture frozen prepared pizza (or the divisions of companies which do) make only that food product; industry recognition of separateness through manufacturers' perceptions and the existence of a trade association; and, most significant, a lack of price sensitivity between retail frozen prepared pizza and other pizzas or frozen foods.[9] We think these factors are adequate to support a finding that retail frozen prepared pizza is the proper product market in this case. [9]

V. "Failing Company"

Assuming a relevant market consisting of sales of frozen pizza throughout the United States, we would have a merger where, as the ALJ found, the acquiring company, Pillsbury, accounted for 15.4% while the acquired company, Fox, accounted for 1.7%. Respondent contends that regardless of these market shares and other aspects of customary analysis of the anticompetitive effects of mergers, this acquisition should be found legal because Fox was a "failing company." The burden of proving such a defense falls, of course, "on those who seek refuge under it." *Citizen Publishing Co.* v. *U.S.,* 394 U.S. 131, 138-9 (1969). We agree with the ALJ that Pillsbury has failed to discharge its burden of proof.

The Supreme Court, in two merger cases,[10] set out the factual predicate which must be present for a company to be "failing" in a

[9] Respondent argues that such broad price sensitivity between pizza and other foods exists. (Respondent Proposed Finding of Fact 64) As support, it cites the testimony of a grocer that when meat prices rose in 1973 and 1974, sales of meat went down and sales of frozen pizza rose correspondingly. We are not sure what the import of this information is since we do not understand respondent to argue that "meat" and frozen prepared pizza are in the same market. In any event, this testimony tells us little since it does not specify the amount of increase in meat prices, or the extent of responding increases in pizza sales.

[10] *International Shoe Company* v. *F.T.C.,* 280 U.S. 234 (1930), and *Citizen Publishing Company* v. *U.S.,* 394 U.S. 131 (1969).

way that its acquisition, regardless of competitive consequences, does not offend the antitrust laws. First, the company must be in such poor competitive condition that "the only alternatives presented are involuntary liquidation, insolvency, or outright sale."[11] It is only at this point in a company's life that the advantage of preservation of the company as a "unit in the competitive system"[12] is overcome by the "seriously injurious consequences otherwise probable"[13] likely to befall the company's employees, creditors and shareholders.[14]

Second, there must have been a good faith effort to determine whether there were other purchasers available whose acquisition of the company would have resulted in less anticompetitive effects.[15] This combines with the critical financial state of the company to make the "failing company" defense a truly "last straw" doctrine. [10]

These descriptions of the essential predicate paint a different picture from the one we have of Fox prior to the acquisition. Fox' total operation probably was losing money in 1976, and the company's total debt had increased and its working capital was depleted. But it had made money in previous years, had a solid and continuing source of credit, and was not on the brink of bankruptcy. Fox recognized all along that its H&R Division had to be sold or liquidated for it to be on sound financial footing over the long term. Of course, Pillsbury did just that as soon as it acquired Fox. Had Fox done this (instead of rejecting an offer to buy the H&R Division in August, 1976) the record indicates that its pizza operation, standing alone, would have been profitable in 1976, the company's worst year. But the financial straits of the H&R Division amounted to neither the imminence of financial ruin nor even "the probability that bankruptcy will ensue."[16] The need to convert one division which, though concededly generating losses, is being kept afloat by another, profitable division, into available capital[17] hardly places a company on the same footing as one facing the virtually immediate advent of receivership.

As to the requirement that Fox make good faith efforts to seek a less anticompetitive alternative, the most we can say about other

[11] *International Shoe, supra,* 280 U.S. at 302.

[12] *Citizen Publishing, supra,* 394 U.S. at 138.

[13] *International Shoe, supra,* 280 U.S. at 302.

[14] *See* Bok, "Section 7 of the Clayton Act and the Merging of Law and Economics", 74 Harv. L. Rev. 226, 340–1 (1960). Only where the sole alternative is the complete discontinuance of the company does an adverse effect on competition due to merger become the "lesser of two evils." *U.S.* v. *General Dynamics Corp.,* 415 U.S. 486, 507 (1974).

[15] *Citizens Publishing, supra* 394 U.S. at 138.

[16] S. Rep. No. 1775, 81st Cong., 2d Sess. 7 (1950).

[17] Pillsbury had no trouble in both selling the H&R Division to the party with whom Fox had negotiated, and overcoming the collection problem at which Fox had balked.

prospective purchasers for Fox is that we don't know if there might have been any. The two companies other than Pillsbury who expressed interest in Fox both started and ended their contacts with Fox in 1975, several months before Pillsbury appeared on the scene. Both nibbles were instigated by the other companies, not Fox. The strongest argument respondents can put forward is that there was "no buyer on the horizon for the losing H&R Division" (Respondent's Answering Brief, p. 24), and that the company's overall prospects were so unpromising that it would have been unlikely that purchasers other than Pillsbury could have been found to acquire either the H&R Division or the entire company. (Respondent's Answering Brief, p. 25) But that simply is not adequate to satisfy the requirement under *Citizen Publishing* that a company contemplating sale make a good faith effort to find a purchaser whose acquisition would be consistent with the purpose of Section 7 to [11] preserve competition.[18] Here, there is nothing in the record to indicate that Fox did anything about seeking prospective acquirers other than to respond to Pillsbury's initiatives.

All in all, Fox's actions were not those of a company trying to avert the threat of total loss to its shareholders, creditors and employees by seeking out the best deal, one which sought reasonable offers most consistent with the purposes of Section 7. Fox remained passive while potential buyers sought it out, did not seek a long-term loan to master a series of temporary problems, and sat on an unprofitable operation which, had it been in dire straits, it could have liquidated. We conclude that while Fox faced serious financial problems, it did not satisfy the stringent standards that apply to a "failing company" defense.

VI. General Dynamics

Complaint Counsel appeals the ALJ's determination that evidence of Fox's weakened status as a competitor caused by its financial instability was sufficient to overcome Complaint Counsel's *prima facie* case. Respondent asserts that recent changes in the retail frozen pizza industry combined with Fox's weakness "from a production standpoint and in the marketplace" (Respondent's Answering Brief, p. 13) compel the conclusion that no substantial lessening of competition will result. The specific marketplace changes to which respondent points involve the entry of large

[18] *See also,* Department of Justice Merger Guidelines, ¶9 (1968), 1 Trade Reg. Rep. (CCH) ¶4510 at 6884, where the failing company defense requires that "good faith efforts by the failing firm have failed to elicit a reasonable offer of acquisition more consistent with the purposes of Section 7 by a firm which intends to keep the failing firm in the market."

national companies which have changed the focus of competition to one emphasizing advertising and heavy promotional activities. Respondent and the ALJ rely principally upon the Supreme Court's decision in *U.S.* v. *General Dynamics Corp.*, 415 U.S. 486 (1974), and a subsequent Court of Appeals case, *U.S.* v. *International Harvester Company*, 564 F.2d 769 (7th Cir. 1977). We do not agree that this case presents an appropriate application of what has come to be called the *"General Dynamics"* defense.

The scope of a proper *"General Dynamics"* defense raises the question of what kinds of evidence are relevant to explore the anticompetitive effects of a merger. In *Brown Shoe Co.* v. *U.S., supra,* the first and landmark exploration of Section 7 enforcement issues, the Court indicated that [12] a rather wide range of economic and other facts would have a bearing on the existence of a violation. But the steady course of decision thereafter demonstrated a recognition by the Court that merger enforcement would have to be streamlined, and key economic facts such as combined market shares relied on to a substantial degree, to permit effective enforcement. *U.S.* v. *Philadelphia National Bank, supra; Ford Motor Co.* v. *U.S.,* 405 U.S. 562 (1972). Continuation of this steady enforcement trend was thrown into doubt in *General Dynamics* where the Court rejected market share and concentration data as conclusive indicators of anticompetitive effect, finding in that case that a merger involving apparent market shares as high as 15.1 and 8.1% [19] did not constitute a violation of Section 7 when all facts about coal production and the changing nature of competition in that industry were taken into account. Since then, companies attempting to defend mergers have often argued (as have respondents in this case) that mergers involving percentage shares previously thought presumptively illegal or likely to produce a finding of anticompetitive effect under Section 7 in fact had no anticompetitive effect when "all the facts" were known. It is important, therefore, to examine exactly what the *General Dynamics* opinion did and did not mean in order to deal with respondents' contentions in this case.

In *General Dynamics,* the Government challenged a merger involving two coal producers, alleging that the proper market was the production and sale of coal in two midwestern areas. The District Court dismissed the complaint and the Supreme Court affirmed on the ground that, while the past production and current sales of the two companies were substantial, the "focus of competition" [20] in the coal industry was on the ability of producers to procure new long-

[19] 415 U.S. at 496.

[20] *Id.* at 501.

term supply contracts. Consequently, the Government's production statistics were of little use in measuring the acquired company's (United Electric's) future ability to compete, since such statistics represented only deliveries under outstanding contracts.[21] In fact, the Court said, the proper measure of competitive strength in the market was "the state of a company's uncommitted reserves of recoverable coal."[22] United Electric, fifth in production, was tenth [13] in reserve holdings, with less than 1% of the reserves held by producers in the larger geographic market alleged by the Government.[23] "Even more significantly", less than 8% of those reserves were uncommitted, and the Court specifically noted that United Electric had no prospect of acquiring new reserves.[24] Moreover, the evidence relied upon by the District Court "could not reflect a positive decision on the part of the merged companies"[25] to influence the competitive picture. The coal industry had changed. Consumption patterns had been altered by the availability of other energy sources. Most coal was purchased by electric utilities, and almost entirely by means of long-term requirements contracts. Such evidence "necessarily and logically implied that United Electric was not merely disinclined but unable to compete effectively".[26]

Finally, the Court distinguished the acquisition of United Electric from that of a "failing company".[27] United Electric would not have gone out of business but for the merger. It would have remained in the market, producing coal, and delivering on its outstanding contractual obligations. The question the Court addressed was rather what the effect of United Electric's continued presence in the market might be, decided that United Electric, without the ability to increase its reserves, had no power to substantially affect competition for new requirements contracts.

Properly viewed, all *General Dynamics* really concluded was that the government had been arguing for a measure of market share which inaccurately portrayed the competitive significance of the merger.[28] Changes in the competitive environment were a reason why reserves rather than past production or current sales were an accurate indicator [14] of market power, but the merger complaint

[21] *Id.* at 501.
[22] *Id.* at 502.
[23] 415 U.S. at 502.
[24] *Id.* at 503.
[25] *Id.* at 506.
[26] *Id.* at 506.
[27] *Id.* at 507–8.
[28] *Cf. U.S.* v. *Amax, Inc.*, 402 F. Supp. 956, 971 (D. Conn. 1975), where the District Court enjoined a contemplated merger after determining that, given the focus of competition in the relevant market (the production of refined copper), the market shares of the merging companies as properly measured (by refining capacity) were such that the merger would substantially lessen competition.

was dismissed essentially because market shares, accurately measured, did not justify a finding of a substantial lessening of competition.

Viewed in that light, Pillsbury cannot validly assert a *"General Dynamics"* defense. None of the evidence presented here in any way undermines the utility of sales figures as a measure of market share or an accurate indicator of market power. Annual sales have been and seem likely to remain the "focus of competition" in the retail frozen prepared pizza industry. The recent entry of larger national companies who engage in intensive advertising and promotional campaigns has changed the industry, but it has not changed the gauge by which a company's market power should be measured. Pizza unlike coal is obviously not an exhaustible natural resource that either company had committed by contract or was in danger of depleting permanently. Small, regional and private label manufacturers remain viable and effective competitors; Fox itself never had any trouble selling as much pizza as it could make. And while competition at the national level may now exist that is beyond Fox's means, it does not follow that Fox at its level does not exert some price pressure on the market leaders. Thus, this is not a case in which market share statistics give "an inaccurate account of the acquisition's probable effect on competition."[29]

General Dynamics speaks to the care with which we must determine what factors to take into account to maximize the accuracy of our prediction of a company's ability to compete in the future. In this case, we think that market shares and concentration ratios are the "primary indicia" of competitive strength,[30] and the proper means to measure it.

Respondent contends that even if the market shares are an accurate measure of present competitive activity and even if Fox were not a "failing company", Fox's financial condition was so poor at the time of the acquisition that it should be considered a seriously weakened competitor in the future. In advancing that argument, respondent relies heavily on *International Harvester.*[31] That case involved Steiger [15] Tractor, Inc. ("Steiger") and International Harvester ("Harvester"), both of which manufactured four-wheel

[29] *Citizens & Southern National Bank, supra,* 422 U.S. at 120.

Retail frozen prepared pizza remains a market, like "groceries or beer" cited in *General Dynamics,* in which "statistics involving annual sales naturally indicate the power of each company to compete in the future." *General Dynamics, supra,* 415 U.S. at 501.

[30] *U.S.* v. *Continental Can Co.,* 378 U.S. 441, 458 (1964).

[31] *U.S.* v. *International Harvester Company,* 564 F.2d 769 (7th Cir. 1977).

drive farm tractors. Steiger supplied such machines to Harvester for resale and also sold them through dealers.[32] In April 1974, Steiger and Harvester entered into an agreement whereby Harvester acquired 39% of Steiger's common stock, and as a result received three directors on Steiger's nine-member Board. The Government challenged this agreement under Section 7; the District Court found for the defendant and the Court of Appeals affirmed.

Steiger's story from 1970 to 1974 is one of a feisty company whose financial outlook was extremely grave and which attempted energetically for several years to bring itself back to fiscal health and finally succeeded. Steiger showed losses in 1970 of over half a million dollars. It obtained bank financing in 1971 but only with the personal endorsement of its chairman, which it had to supplement with money from a venture capital firm. Both loans were called in early 1972 and Steiger turned for capital to customers, and finally to a factor (who charged almost twice the prime lending rate at the time). In 1973, Steiger's balance sheets showed an improvement, but the company was carrying a huge load of costly debt.

The purchase agreement provided that Harvester could in no way limit or control Steiger's business activities. The parties simultaneously executed a five-year Manufacturing Agreement, with Harvester obligated to buy a certain number of tractors assembled by Steiger through 1979.

The Court of Appeals, in upholding the transaction, relied principally on Steiger's precarious financial condition at the time of the agreement which "placed it at a competitive disadvantage,"[33] and which was cured by the influx of funds from Harvester.[34] Moreover, the court found that the [16] agreement had made Steiger a more aggressive, independent competitor, whose presence contributed to a marked decrease in concentration in the relevant markets, evidenced by "intensified price competition."[35] The Court read *General Dynamics* not to be limited to situations involving a depletable natural resource, nor even to situations where statistics concerning past sales are a misleading indicator of market power, but to extend to all cases where weakness, financial or otherwise, impairs a company's ability to compete.

[32] In 1973, Steiger manufactured four-wheel drive tractors for itself and others accounting for 19% of industry shipments; Harvester's own production represented 6%. The four-firm concentration ratio was 83%. Steiger also produced 7% of all high powered farm tractors while Harvester's production was 27%, and the four-firm concentration ratio in that market was 73%. 564 F.2d at 771.

[33] 564 F.2d at 776.

[34] The court rejected the notion that Harvester had to be shown to be the *only* source of financing because, i said, defendants did not rely on the failing company doctrine. 564 F.2d at 779. The Court added that there wa evidence that Harvester was indeed the only purchaser, but that was inferred from the "onerous options otherwis available to Steiger", not from any evidence that Steiger sought out other bids. 564 F.2d at 779.

[35] 564 F.2d at 778.

Inclusion of financial weakness as a separate factor or defense — other than in a failing company situation, of course — raises serious antitrust policy problems. First, there may be a sort of double counting in that financial weaknesses may already be reflected in a market share of the troubled company that is lower than it would have been but for the financial problems. Second, the issue of financial weakness is extremely difficult to handle in court, and susceptible to invented claims and vague expert testimony generating factual issues that the courts are not well equipped to measure. Third, if all sorts of company "weaknesses" or structural market changes operating to the disadvantage of particular companies, can overcome a *prima facie* case of illegality, then the whole valuable trend in merger enforcement toward streamlining cases by concentrating on properly measured market shares and concentration ratios will be undermined. This is not to say that in a close case, financial weakness cannot be taken into account along with many other factors in predicting the market consequences of a merger, but rather that there ought not be a broad *"General Dynamics"* defense that may be relied upon to overcome clear instances of illegality based on market shares and concentration ratios.

In addition, there is the issue of why the financially weak company, as a result of diminished market shares, should have an option to sell out to a competitor. If money problems are plaguing the firm, money can cure them and there seems no reason to believe that the money cannot be obtained from a variety of sources other than a competitor. While the court did find in *International Harvester* that Harvester was "the only practicable source," there was no evidence that Steiger had shopped around for another purchaser or source of funds which would have produced a less [17] anticompetitive result.[36] If Steiger's money troubles were so severe that its existence was in question, then, like any "failing company," it should have been required to seek out the least anticompetitive alternative purchaser. Certainly, there is little logic or fairness in imposing a rigorous requirement of search for a preferred purchaser on a 'failing company" on the brink of extinction and not on one that's nerely "troubled."

For all of the reasons cited above, we conclude that if *International Harvester* reads *General Dynamics* to extend to a wide array of stances where "financial weakness" constitutes a defense for

[36] See note 34, *supra*, p. 15. Interestingly, in *General Dynamics, supra*, the Supreme Court particularly noted : it was only additional uncommitted reserves which could have restored the acquired company's potential as a petitor and that the company had "neither the possibility of acquiring. . .nor the ability to develop" those rves. 415 U.S. at 503.

otherwise clearly illegal mergers, we respectfully decline to follow it.[37]

The circumstances surrounding the "financial weakness" of Fox prior to its acquisition by Pillsbury are instructive in demonstrating why such factors ought not to lead to a finding of no violation of Section 7. Fox had serious financial difficulties, but there were reasons to believe they were temporary, and certainly they were susceptible to solutions other than sale to a horizontal competitor. Avenues of financial support other than its one line of credit were never explored. Other potential acquisition candidates were not canvassed prior to the acquisition by Pillsbury. Finally, Fox almost certainly could have solved its financial problems by selling off its H&R Division and eliminating the drain on its otherwise profitable pizza business — as Pillsbury in fact did immediately after completion of the merger. Thus, even if evidence of financial weakness were to constitute some sort of defense in Section 7 enforcement — an approach which we believe should rarely, if ever, be followed except in a "failing company" context — Fox's financial difficulties were not of a sort to justify such a defense.

VII. Absence of Significant Anticompetitive Effect.

Although Fox does not qualify as a "failing company" and is not entitled to any variation of the *"General Dynamics"* defense, we nevertheless find that the Pillsbury-Fox merger does not violate Section 7 because it is not likely to have significant anticompetitive effects. [18]

Pillsbury ranked third in 1976 with 15.4%.[38] Fox's share had decreased from 2.4% in 1975 to 1.7% in 1976. On a strict percentage basis, these market shares fall in the gray area at the edge of potential illegality under the Department of Justice guidelines for horizontal mergers,[39] but a finding of a violation would not be entirely unprecedented.[40] We note in addition, however, that while

[37] There is an alternative reading of *International Harvester* limiting it to its facts, *i.e.*, a partial stock acquisition which did not give the shareholder company control. Such reading would render *International Harvester* simply inapposite to this case.

[38] Respondent contested the market share figures used by the ALJ. Complaint counsel had argued that Pillsbury ranked second in 1976 with 18.28%, while respondents agreed to the No. 2 ranking but thought the market share was only 13.7%. Our disposition of this case would be the same whichever set of figures is used.

[39] Department of Justice, Merger Guidelines, ¶5, 6 and 7 (1968), 1 Trade Reg. Rep. ¶4510 at 6884 (1971).

[40] *Cf. U.S.* v. *Aluminum Co. of America*, 377 U.S. 271 (1964); *Stanley Works* v. *FTC*, 469 F.2d 478 (2d Cir. 1972). Of course, mergers have been found illegal where the combined market share was less than the 17.1% involved here. See *e.g.*, *Beatrice Food Co.* v. *FTC*, F.2d 303 (7th Cir. 1976) (7.6 and 2.3%); *Liggett & Myers, Inc.* v. *FTC*, 567 F.2d 1273 (4 Cir. 1977) (10.99% and 4.4%). This case is different, however, because of the small size and insignificant competitive potential of the acquired company.

the four-firm concentration ratio for the national frozen pizza market was found by the ALJ to be 60.8%,[41] barriers to entry, even for fairly small companies, were moderate to low.

Fox was not only small but it was in no sense a company with special competitive potential which might lead to a conclusion that modest market shares understated the future competitive significance of the acquired company. Thus, in *U.S.* v. *Aluminum Co. of America,* 377 U.S. 271 (1964), the acquisition of a company accounting for only 1.3% of sales was nevertheless found illegal because it was an aggressive independent competitor, a pioneer in efficient research and sales, and possessed of special aptitudes and skills in the relevant product line. Here, Fox had been a price-oriented marketer, but there's no evidence that it was sufficiently aggressive to constitute a destabilizing price cutter in the market. [19]

As Commissioner Dixon rightly points out in his dissenting opinion, the Supreme Court has found that a trend to concentration can be an important factor in merger analysis, occasionally leading to a finding of illegality even when small horizontal acquisitions are involved. See *Brown Shoe Co.* v. *U.S., supra,* 370 U.S. at 345-6. Using figures most favorable to complaint counsel (*supra,* note 41), the four firm concentration ratio in retail frozen pizza sales increased from 55.48% in 1974 to 62% in 1976, and the seven firm concentration ratio increased from 70.74% in 1973 to 80.74% in 1976 — significant increases in concentration. In dealing with concentration trends, however, the courts have further stated that the underlying rationale for taking such trends into account involves the necessity of preserving the small firm as a vehicle for "eventual deconcentration" of the market. *Philadelphia National Bank, supra,* 374 U.S. at 365, n. 42; *cf. Stanley Works* v. *FTC, supra,* 468 F.2d at 508. Here, there is simply no reason to believe that Fox could have combined with other small frozen pizza manufacturers to challenge larger companies in the market. Also, given Fox's size and the nature of its assets, there is no reason to believe that Fox, if acquired by a company outside the market, could have constituted a springboard to permit a new entrant to challenge the market leaders. Despite a trend toward concentration in this industry, it is clear that *de novo* entry is feasible and has actually occurred.[42] Thus it would appear that an outsider could as easily achieve a significant market position through complete *de novo* entry as through the acquisition of Fox,

[41] Various concentration ratios were introduced into evidence, depending on whether SAMI or Market Research Corporation of America data was used, ranging from a high of 4:62% in 1976 to a low of 4:49.3% in 1976. D. 100; CX 55, 60, 64.

[42] See note 3, *supra,* p. 3.

and, as a result, the importance of preserving Fox as an eventual deconcentrator fades.

There is no other reason to believe that Fox's declining 1.7% of national sales in 1976 does other than accurately portray its competitive significance. The fact that its entire assets were exchanged for approximately $3 million worth of common stock is some indication that no large premium was paid here by Pillsbury to eliminate a significant competitive factor.

Horizontal mergers have never been viewed as illegal *per se* under the antitrust laws even though a merger predictably will eliminate competition more completely than any price-fixing or other anticompetitive agreement.[43] Long-term competitive considerations require preservation of [20] ease of entry, and opportunity for businessmen to take entrepreneurial risks. The other side of that coin is a largely unarticulated policy, a clear corollary to the first, which would preserve exit opportunities where significant anticompetitive results do not occur. It is essential that the owners of very small businesses with slight competitive potential have some reasonable flexibility to sell out. This set of considerations is particularly compelling where the small acquired asset is a family-owned business which has come upon uncertain and perhaps adverse business conditions. Professor Areeda summarized relevant factors that attend that situation in the following terms:

> The retiring entrepreneur may lack confidence in his successors or may prefer the security of portfolio diversification. Or a firm may be impelled toward merger by the fact or fear of relative decline. The actual or prospective difficulties might be in management, research, marketing, capital, labor, or anything else that affects a firm's fortune. Sale of the company as a going business may cause minimum disruption to owners, managers, suppliers, customers, employees, and communities. To facilitate exit when it is desired may indeed facilitate entry. The likelihood of exit with minimum loss or maximum gain increases the attractiveness and reduces the risk of entering a market.[44]

Congress was similarly aware of the importance of designing antimerger legislation so as not to render unduly difficult market exit by very small firms. When Section 7 was amended to extend to asset as well as stock acquisitions in 1950[45] the question of the new

[43] *Cf. U.S.* v. *Socony-Vacuum Oil Co., Inc.*, 310 U.S. 150 (1940), which established a *per se* rule against "[a]ny combination which tampers with price structures." 310 U.S. at 221.

[44] Areeda, *Antitrust Analysis*, 2nd Ed., para. 617(h) at p. 690 (1974).

It is worth noting that this array of factors are some of the reasons why mergers among small companies, or acquisition by a large company of a very small company, should not be treated under *per se* rules or even found to violate Section 7. Citation of this variety of factors is not meant to suggest that each should properly be the subject of proof in a merger case.

[45] Pub. Law 899, 64 Stat. 1125; (1950).

statute's impact on the opportunity of small business to move in and out of a market was addressed: [21]

Furthermore, the Supreme Court and the Federal courts have not applied the present strict language of Section 7, even in cases of stock acquisition, so as to prevent a small corporation from selling its business *or* of merging with another small business. The Supreme Court has only applied the present language of Section 7, even in the case of stock acquisitions, to large transactions which would substantially lessen competition, or tend to create a monopoly. [emphasis added][46]

As noted earlier in this opinion, the law properly sets a demanding standard before a "failing company" defense can be asserted successfully, and we believe any additional relaxation in previous Section 7 enforcement approaches that may be thought to be generated by the *General Dynamics* decision be given a very limited scope. These narrow interpretations of two possible "exceptions" to general antitrust principles can be more fairly maintained if there is an appreciation that mergers between two small companies, or between a large and a very small company, do not necessarily violate Section 7. We believe it is better antitrust policy to delineate a fairly clear line beneath which mergers between horizontal competitors will not be declared illegal than to create vague and potentially sweeping exceptions likely to complicate and delay enforcement actions. We believe the following describes an acquisition that falls below that line: the acquisition by a non-dominant[47] company of a very small competitor (in absolute terms), lacking any special competitive potential and with a declining 1.7% market share, where there are no significant barriers to entry and when there is no reason to believe that the acquired company, in other hands, would have been a vehicle leading to less concentration or an increase in competition.

FINAL ORDER

This matter has been heard by the Commission upon the appeals of complaint counsel and respondent from the initial decision and upon briefs and oral argument in support of and in opposition to the

[46] H. Rep. No. 1191, 81st Cong., 1st Sess. 7 (1949). This point was also made repeatedly in the floor debates. *See, e.g.,* 96 Cong Rec. 16435 (1950) ("Any action by the Federal Trade Commission designed to halt mergers of an inconsequential nature would not be in accordance with the language of the bill and would not be upheld by the courts.") [Remarks of Sen. O'Conor]; 96 Cong. Rec. 16441 (1950); [Remarks of Sens. Kem and O'Conor]; 96 Cong. Rec. 16444 (1950) [Remarks of Sen. Kefauver].

[47] We have no occasion to define here all the circumstances in which an acquiring firm would be so large that acquisition of even such an insignificant competitive factor as is involved here might violate Section 7. An obvious example would be a situation in which the acquiring firm is a monopolist. Another example might involve a "dominant firm", sometimes defined to possess between 20 and 30% of a relevant market, *cf. Philadelphia National Bank, supra,* 374 U.S. at 364–5 n.41, and standing first or a very close second in that market.

appeals. For the reasons stated in the accompanying Opinion, the Commission has denied the appeals.

It is ordered, That pp. 1–50 of the initial decision of the administrative law judge be adopted as the Findings of Fact of the Commission, except insofar as they are inconsistent with the accompanying opinion. Pages 51–63 of the initial decision are not adopted.

It is further ordered, That the complaint be dismissed.

Commissioner Dixon dissents.

IN THE MATTER OF

NATIONAL INDUSTRIES, INC., ET AL.

ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket 8859. Complaint, July 15, 1971 — Dismissal Order, June 18, 1979

This order dismisses a complaint charging a Louisville, Ky. firm and its wholly-owned subsidiary with illegally imposing geographic restrictions on licensed bottlers of their soft drink products, on the grounds that the companies are no longer engaged in the soft drink business or the practices which were the focus of the complaint.

Appearances

For the Commission: *Ronald L. Bloch.*

For the respondents: *Charles Kadish, Breed, Abbott & Morgan,* New York City and *Paul N. Kiel,* Fuqua Industries, Inc., Atlanta, Ga.

COMPLAINT

The Federal Trade Commission, having reason to believe that National Industries Inc. and its wholly-owned subsidiary, Cott Corporation, each hereby made and sometimes hereinafter referred to as respondent(s), have violated the provisions of Section 5 of the Federal Trade Commission Act (15 U.S.C. 45), and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint, stating its charges in that respect as follows:

PARAGRAPH 1. For the purposes of this complaint, the following definitions shall apply:

(a) Bottler — any individual, partnership, corporation, association or other business or legal entity which purchases respondents' concentrate for use in the manufacturing and sale, primarily at wholesale, of pre-mix or post-mix syrups or soft drink products or who purchases pre-mix or post-mix syrups or soft drink products for resale, primarily at wholesale;

(b) Central warehousing — a method of distribution in which soft drink products are received at a storage facility and either resold or delivered to retail outlets or wholesalers;

(c) Concentrate — the basic soft drink ingredient sold to bottlers by respondents, which is combined with water and other ingredients for packaging in bottles or cans for sale and distribution as soft drink products, or is used to make post-mix and pre-mix syrups;

(d) Consignment — a form of distribution in which the consignor retains title, dominion, bears all risks of loss and delivers his products to the consignee who is indistinguishable from a salesman or agent;

(e) Place of business — the location of any facilities available to a bottler without regard to customers or geographic area for production or service in the conduct of business operations, to include but not limited to business headquarters, branch sales offices, warehouses and garages, but specifically excluding the plant at which a bottler combines concentrate with water, and possibly other ingredients, for the packaging of soft drink products;

(f) Post-mix syrup — soft drink concentrate which is used in fountain dispensing or vending equipment and is usually sold by bottlers in steel tanks. A typical post-mix system draws one ounce of syrup from a five-gallon tank and mixes it at the point of sale with six ounces of carbonated water to produce 600 six-ounce finished soft drink servings per tank;

(g) Pre-mix syrup — although essentially the same syrup as post-mix, a pre-mix system differs from a post-mix system in that it draws from a five-gallon tank a serving of soft drink products containing both syrup and carbonated water to produce 100 six-ounce finished soft drink servings;

(h) Soft drink products — nonalcoholic beverages and colas, carbonated and uncarbonated, flavored and non-flavored, sold in bottles and cans, or through pre-mix and post-mix systems or the like.

PAR. 2. Respondent National Industries Inc., is a corporation organized, existing and conducting its business under and pursuant to the laws of the Commonwealth of Kentucky. It maintains its office and principal place of business at 510 West Broadway, Louisville, Kentucky. In 1968, respondent National Industries Inc. had net sales of $353,310,000 and assets of $283,771,000.

Respondent Cott Corporation, a wholly-owned subsidiary of National Industries Inc., is a corporation organized, existing and conducting its business pursuant to the laws of the State of New Hampshire. It maintains its office and principal place of business at 197 Chatham St., New Haven, Connecticut; owns and operates a concentrate manufacturing plant at Hamden, Connecticut; and operates soft drink bottling plants at South Portland, Maine, Millis and Somerville, Massachusetts, Pawtucket, Rhode Island, New

Haven, Connecticut, Manchester, New Hampshire, Bronx, New York, Elizabeth, New Jersey, Braddock, Pennsylvania and Miami, Florida. In 1968, respondent made sales to over 100 domestic bottlers located in 29 States throughout the United States.

PAR. 3. Respondent National Industries Inc., through various subsidiaries, is engaged in diverse businesses including sale of soft drink products and concentrate, dairy products, laboratory furniture, energy products and steel service centers. Its Consumer Products Division, with which respondent Cott Corporation is affiliated, accounted for $215,383,000, or 57% of total revenue in 1969.

Respondent Cott Corporation is engaged principally in the manufacture and sale of soft drink products and concentrate under its name, Cott, and under the names of its wholly-owned subsidiaries, Clicquot Club Company and Mission of California, Inc. In addition to its business as a bottler, respondent Cott sells soft drink products and concentrate to over 100 bottlers, who purchase under license to produce and sell soft drink products under such trade names of respondent as "Cott," "Clicquot Club," "Mission," "Quiky," "Energade" and "Big Giant Cola." Bottlers combine the concentrate with water and other ingredients and then package the mixture in bottles and cans for resale as soft drink products to retailers.

PAR. 4. Respondents are engaged in "commerce" within the meaning of the Federal Trade Commission Act (15 U.S.C. 44) in that National Industries Inc., through its wholly-owned subsidiary Cott Corporation, causes a continuous flow of interstate commerce in soft drink products and concentrate to exist between Cott Corporation headquarters and production facilities in New Haven and Hamden, Connecticut, and the numerous bottlers and retailers located throughout the United States which purchase their products.

PAR. 5. In the course and conduct of their businesses, respondents, except to the extent limited by the acts, practices and methods of competition hereinafter alleged, have been and are now in competition with other corporations, firms, partnerships and persons engaged in the manufacture, processing, distribution and sale of soft drink products in commerce.

PAR. 6. Respondents have hindered, frustrated, lessened and eliminated competition in the distribution and sale of pre-mix concentrates and soft drink products sold under their trade names by restricting their bottlers from selling outside of a designated geographical area. This restriction is set forth in the franchise agreement between respondents and their bottlers.

A typical agreement between respondent Cott Corporation and its bottlers provides that the bottler agrees:

To aggressively merchandise, promote, advertise and maintain the sales and distribution of Products in the territory covered by this Franchise Agreement, and to restrict distribution of Products produced by BOTTLER within the territory covered by this Franchise Agreement, and not permit the shipment, either directly or indirectly, of Products produced by BOTTLER into territories outside of the territory covered by this Franchise Agreement. In the event any other authorized franchisee of Products should, without authority of COMPANY, ship or permit to be shipped, any Product or Product Base into the exclusive territory covered by this Franchise Agreement, (except where said other authorized franchisee sold and delivered said Product Base to a customer within their territorial limits) COMPANY agrees to take appropriate action to prevent the continuation of such unauthorized acts, but shall not be liable in damages to the BOTTLER by reason of such unauthorized shipments, COMPANY'S obligations in this respect being limited to the exercising of the highest good faith to prevent such act or acts.

PAR. 7. The aforesaid agreements used by respondent Cott have had, and may continue to have, the following effects:

(a) Competition between and among respondent Cott's bottlers in the distribution and sale of "Cott," "Clicquot Club," "Mission," "Quiky," "Energade" and "Big Giant Cola" brands of soft drink products has been eliminated;

(b) Competition between and among Cott's bottling operations and its bottlers in the distribution and sale of Cott soft drink products at the wholesale level has been eliminated;

(c) Innumerable retailers and other customers have been deprived of the right to purchase "Cott," "Clicquot Club," "Mission," "Quiky," "Energade" and "Big Giant Cola" brands of soft drink products from the bottler of their choice at a competitive price; and

(d) Consumers of "Cott," "Clicquot Club," "Mission," "Quiky," "Energade" and "Big Giant Cola" brands of soft drink products have been deprived of the opportunity of obtaining such products in an unrestricted market and at competitive prices.

PAR. 8. Respondents' contracts, agreements, acts, practices and methods of competition aforesaid have had and may continue to have, the effect of lessening competition in the advertising, merchandising, distribution, offering for sale and sale of pre-mix concentrates and soft drink products; deprive, and may continue to deprive, the public of the benefits of competition in the purchase of soft drink products; and constitute unfair methods of competition and unfair acts or practices, in commerce, in violation of Section 5 of the Federal Trade Commission Act.

(Official National Industries Inc. Stationery)

(Date)

Dear

The Federal Trade Commission has entered an order against National Industries Inc. and Cott Corporation which among other things prohibits them from limiting, allocating or restricting the territory, persons or class of persons to whom our bottlers may sell. In addition, the order prohibits National Industries Inc. and Cott Corporation from restricting the location of the bottler's place of business or requiring an allocation of fees between one bottler and other bottlers for sales to any particular customer or in any geographical area.

National Industries Inc. and Cott Corporation are also prohibited from refusing to sell or threatening to refuse to sell to any bottler anything used in the manufacture and sale of soft drink products. Furthermore, National Industries Inc. and Cott Corporation are prohibited from requiring or requesting any bottler to, in any manner, inform them of the territories in which, or the person or class of persons (including but not limited to central warehousing customers) to whom the bottler sells, or attempts to sell, soft drink products, or pre-mix or post-mix syrups. A copy of the order is attached.

The Federal Trade Commission has expressed its intention to determine the effect upon the marketing of soft drink products caused by the attached order by ascertaining at some future date the extent to which sales of soft drink products by bottlers extend to customers outside of previously established, but now prohibited, territorial restrictions.

Very truly yours,

Initial Decision Dismissing Complaint by Joseph P. Dufresne, Administrative Law Judge

April 23, 1979

Preliminary Statement

The complaint in this matter is one of eight which issued against bottlers of soft drinks on July 15, 1971, challenging the geographic restrictions on franchisees established by the bottler/franchisors. Of these complaints, those against *The Coca-Cola Company, et al.* (Dkt. 8855) and *PepsiCo, Inc.* (Dkt. 8856) have been litigated and decisions [2] by the administrative law judge and the Commission have issued. The decisions against The Coca-Cola Company, et al. and PepsiCo presently are on appeal to the U.S. Circuit Court of Appeals for the District of Columbia.

The proceedings in connection with the complaints against the six other bottlers charged (*i.e. Crush International Limited, et al.* (Dkt. 8853) *Dr Pepper Company* (Dkt. 8854), *The Seven-Up Company* (Dkt. 8857), *Royal Crown Cola Company* (Dkt. 8858), *National Industries/Cott* (Dkt. 8859) and *Norton Simon, Inc./Canada Dry* (Dkt.

8877)) have been held in abeyance pending the outcome of the appeals in the *Coke* and *Pepsi* cases. No adjudicative hearings have been held in these six matters. (*See* "ORDER RE INTENTIONS OF RESPONDENTS IN UNLITIGATED 'BOTTLER' CASES" dated December 15, 1975, and "ORDER RE SUSPENDING HEARINGS IN SIX REMAINING 'BOTTLER' CASES PENDING APPELLATE COURT REVIEW OF COMMISSION'S COCA-COLA AND PEPSICO DECISIONS" dated September 19, 1978.)

DISCUSSION

In a letter/motion requesting dismissal of this complaint as to National, counsel for respondents National Industries, Inc. and Cott Corporation advised that neither firm is engaged any longer in the soft drink business or in the practices which are the subject of this matter. Commission counsel does not oppose the letter/motion. Counsel for respondents advised that the acquirer of Cott is dissolving it. (*See* letter from Charles Kadish, Esq. to me dated February 14, 1979, and "ORDER PLACING LETTER APPLICATION FOR DISMISSAL ON THE PUBLIC RECORD" dated February 27, 1979.) Commision counsel has advised that there is no information as to whether a "New Cott Corporation," which is reported to be conducting the soft drink business of respondent Cott, is engaging in the challenged practices. (*See* "COMPLAINT COUNSEL'S RESPONSE TO RESPONDENT'S MOTION TO DISMISS THE COMPLAINT AS TO NATIONAL INDUSTRIES, INC.," dated April 18, 1979.)

In these circumstances, it would be to the interest of the public, the Commission and respondents if the complaint were dismissed. Accordingly, and pursuant to authority contained in Commission Rules 3.22(a)(e), 3.24(a)(2), 3.42(c) and 3.51, [3]

ORDER

It is ordered, That the complaint in Dkt. 8859 against respondents National Industries, Inc., and Cott Corporation be, and it is hereby, dismissed.

FINAL ORDER

The administrative law judge filed his initial decision in this matter on April 23, 1979, dismissing the complaint against respondents National Industries, Inc. and Cott Corporation on grounds that neither respondent is now engaged in the soft drink business nor in the practices which were the focus of the complaint. No appeal from the initial decision was filed.

The Commission having now determined that the matter should not be placed on its own docket for review, and that the initial decision should become effective as provided in Section 3.51(a) of the Commission's Rules of Practice,

It is ordered, That the initial decision and order contained therein shall become effective on June 18, 1979.