

MERGER ANTITRUST LAW

LAW 1469
Georgetown University Law Center
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Tuesdays and Thursdays, 3:30 pm – 5:30 pm
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Class 16: U.S. Sugar/Imperial Sugar (Unit 7)

In this class, we will critique the parties' performance in U.S. Sugar/Imperial Sugar. We will start with the most important reason why the merging parties won the case (think "hearts," not "minds"), then turn to what the DOJ did wrong, and end with what the merging parties did right. My assessment is that the defense's account of how the acquisition could improve Imperial's operations helped make its competitive analysis persuasive. That assessment is different from the court's holding: the DOJ lost because it failed to establish a relevant market, not because the court balanced proven efficiencies against proven competitive harm.

The assignment requires close reading of 111 pages of reading materials and 12 class note slides. An additional 57 pages are assigned for skimming. Skimming is part of the assignment, but does not require close reading. Material identified below as optional or suggested review may be skipped.

Supply-side switching. Before you read the *U.S. Sugar* opinion, it is useful to distinguish the market boundary from the firms and productive capacity that constrain competition within it. Under the Merger Guidelines, demand-side substitution determines market boundaries. Supply-side switching occurs when a higher price induces firms to redirect production toward the product whose price has increased. A producer need not currently sell that product to become a meaningful competitive constraint. The Guidelines include current suppliers, firms committed to entering in the near future, and qualifying rapid entrants as market participants. Recognizing a rapid entrant does not by itself determine its share; the measure must reflect its competitive significance. Rapid entrants must be very likely to enter rapidly, have a direct competitive impact, and do so without significant sunk costs; idle capacity or technical capability alone is not enough. Firms whose entry requires more time or significant sunk costs are evaluated separately; other entry, expansion, and repositioning belong in the competitive effects analysis. Courts have sometimes incorporated supply-side substitution into market definition itself. These approaches can produce different concentration measures even when they address the same underlying source of competition. Read the Unit 7 class notes' explanation of these distinctions (slides 3-6).

Read the provisions on market participants and market shares (2010 Horizontal Merger Guidelines, §§ 5.1-5.2, pp. 229-32; 2023 Merger Guidelines, § 4.4, pp. 233-36). These provisions explain when prospective suppliers count as market participants and how sales or capacity can measure their competitive significance. The 2010 provisions were available at the time of the *U.S. Sugar* trial; the 2023 provisions provide a subsequent comparison.

The pencil example illustrates the distinction. No. 2 and No. 4 pencils are assumed not to be substitutes for customers, but manufacturers can use the same equipment to make either. Ace and Benny, the only current No. 4 producers, make 400 and 300 units, respectively. Four other manufacturers each produce 2,500 No. 2 pencils and would switch 10%, or 250 units each, to

No. 4 pencils in response to a 5% price increase. Enterprise's capacity is fully committed by contract and is excluded. Holding Ace's and Benny's No. 4 output constant, the assumed available supply is therefore 1,700 units: their existing 700 units plus 1,000 units from the four rapid entrants. Ace and Benny have a combined share of 41.18%; the postmerger HHI is 2,561, with an increase of 830. These figures trigger the structural presumption under both the 2010 and 2023 Merger Guidelines. The calculation already credits the assumed switching response, but that response is insufficient to bring the concentration measures below the presumption thresholds. Read the Unit 7 class notes' example and its implications for the *Philadelphia National Bank* presumption (slides 7-9).

The contrasting calculation uses the same production figures and switching assumptions, but counts all production of both grades by the participating firms. Enterprise remains excluded. This broader measure counts 10,000 units from the four outside producers even though their assumed switching response is only 1,000 units. It also counts Ace's and Benny's No. 2 production, although their No. 4 output is held constant. The total rises to 11,400 units, the merging firms' combined share falls to 12.3%, and the HHI increase falls to 75, making the merger appear nonproblematic. The point is not that the firms would switch different amounts in two versions of the hypothetical. Counting production that would not switch overstates the outside firms' competitive significance and understates that of the merging firms. The judicial discussion explains why some courts consider supply substitution in defining market boundaries; the numerical comparison shows why recognizing that constraint does not justify counting all production equally (slides 10-12).

Successful switching also requires access to customers, distribution, and any necessary services, as well as an incentive to sell at the higher price after accounting for additional production and selling costs and the profits forgone on the product displaced. Positive accounting profits on the new product do not establish that switching is profitable if the firm would earn more by continuing its existing production. Read the concluding discussion of these limits in the Unit 7 class notes (slides 13-14). In *U.S. Sugar*, much of the relevant supply evidence concerns redirecting shipments of the same product, using available capacity, or expanding output, rather than changing the product manufactured. The common point is that historical sales may not measure the full prospective constraint. The analytical treatment nevertheless depends on what the supplier would do, how quickly, and at what cost.

The transaction and the defense's business account. *U.S. Sugar* grows sugar cane and operates a refinery in Florida; it is a member of United, a separate marketing cooperative that sets prices and markets and sells its members' sugar. United's authority over those activities does not give it control over the member companies. Imperial's principal asset was its Port Wentworth refinery in Georgia. Imperial relied heavily on imported raw sugar and operated below capacity. The defense connected the acquisition to a more secure domestic raw sugar supply, increased refinery utilization and output, transportation savings, and greater reliability through United's distribution network. These were concrete operational propositions, supported by witnesses and documents, rather than a general assertion that larger firms are more efficient. Skim the press release announcing the U.S. Sugar/Imperial Sugar transaction (pp. 5-7). The court's findings develop Imperial's operating problems and the anticipated benefits (pp. 58-61).

That account matters to our critique of the prosecution. A persuasive response to claimed benefits examines whether they are verifiable, achievable without the merger, likely to reach customers, and sufficient to prevent the threatened competitive harm. An objection about merger

specificity is more useful when supported by evidence about practicable alternatives, such as a supply contract or independent investment. This does not shift the legal burden to the DOJ to disprove every claimed benefit. The district court did not adjudicate a formal efficiencies or failing firm defense; its favorable findings about the transaction help explain the litigation setting in which it rejected the government's case.

The DOJ's theory and its burden of proof. The DOJ alleged that the acquisition would remove competition between United and Imperial in sales of refined sugar to wholesale customers in the Southeast and in a smaller Georgia-centered region. Its case combined concentration evidence with allegations of lost head-to-head competition and an increased risk of coordination. These were the government's allegations, not adjudicated findings of harm. Market definition was therefore essential to its effort to invoke the *Philadelphia National Bank* presumption: high shares and concentration have significance only if the market and the measurement of participation are supported. Skim the DOJ's press release and complaint challenging the deal (pp. 9-37).

At this point, I suggest read the district court's entire Memorandum Opinion (pp. 38-97). The narrower references below highlight particular issues within that assignment.

Distributors and customer groups. The DOJ treated distributors as customers of producers rather than independent competitors. The court found that distributors also competed against refiners for wholesale business, obtained sugar from alternative suppliers, and could sell successfully against their own suppliers. Their vertical relationship with refiners did not establish that refiners controlled their competitive conduct. Including distributors requires care in attributing sales so that the same sugar is not counted twice, but excluding them required evidence that their rivalry would not constrain the merged firm. The court credited the defense's account of that rivalry, and the DOJ acknowledged that it lacked the evidence to prevail if distributors were included. Read the findings and product market analysis together (pp. 65-69, 81-85).

The DOJ also grouped industrial, retail, food service, and distributor customers together. Evidence of separate sales teams and different sales mixes raised a material issue about whether these customers faced similar competitive alternatives. Those business practices do not by themselves prove separate antitrust markets. The weakness was the absence of an adequate evidentiary basis for the government's aggregation. A sound analysis would establish why the groups could be combined or examine them separately and determine whether the result changed. The court's findings and analysis explain this second product market problem (pp. 70-71, 85-86).

Geographic markets and supply responses. The distinction between supplier-location and customer-location markets is particularly important here. A supplier-location market groups the locations from which sales are made. A customer-location market groups customers who can be targeted with worse terms, wherever their suppliers happen to be located. Thus, a refinery outside the Southeast can participate in a market for sales to customers inside the Southeast. For a customer-location market, the hypothetical monopolist controls all sales of the relevant product to customers in the region, including sales by suppliers located elsewhere. Existing cross-boundary shipments alone do not disprove such a market. The hypothetical monopolist test asks whether the specified hypothetical monopolist could profitably impose a small but significant and nontransitory price increase, taking account of the relevant customer substitution and arbitrage opportunities. It does not ask merely whether some sugar already travels long distances.

For a refresher, you might find it helpful to review geographic market definition in the current Unit 3C class notes (slides 43-64).

The defense nevertheless supplied important evidence of purchases from distant suppliers, additional available supply, customers' ability to arrange transportation, and planned expansion. The district court found the DOJ's selected regions inconsistent with commercial realities and criticized the independent support for their selection. Our critique must distinguish that holding from the more precise economic questions. Market definition, the identification and measurement of participants, and competitive effects are separate steps. The DOJ needed a convincing explanation of why the defense's supply evidence did not defeat its predicted harm, even if that evidence did not require enlarging a properly specified customer-location market. More than one market can satisfy the HMT. Read the geographic findings and analysis (pp. 71-77, 87-92).

The same distinction limits what can be inferred about concentration. The court credited testimony that excluding distributors overstated shares and concentration, but it did not calculate corrected HHIs or reach the competitive effects component of the DOJ's prima facie case. It would therefore overstate the holding to say that the court found a recalculated market unconcentrated or that an adjusted HHI necessarily defeated the presumption. The prosecution also needed supported alternatives if a central premise failed. Its distributor concession and its insufficiently developed USDA South alternative illustrate the cost of lacking such a fallback (pp. 84-85, 90-92).

Experts and industry witnesses. An expert's credentials, admissibility, and persuasive force are different matters. The court preferred Nicholas Hill's testimony to David Rothman's and criticized the support for Rothman's analysis. It did not exclude Rothman; the defendants did not pursue their qualification objection in their post-trial briefing. Prior judicial criticism of an expert warrants attention to the reasoning and methodology involved, rather than automatic disqualification. The broader preparation issue is whether the economic analysis fits the business evidence and can answer the opposing account. Read the discussion of the economists with these distinctions in mind (pp. 62-65).

As the district court describes it, the Federal Sugar Program supports domestic producers through price-support loans and manages supply through domestic marketing allotments, tariff rate quotas, and arrangements governing Mexican imports. Expanded allotments or additional low-duty imports can increase available supply and affect prices. These national supply-management tools do not mean that USDA sets individual refiners' contract prices or necessarily detects and prevents harm to particular regional customers. That distinction matters when evaluating Fecso's testimony and the court's reliance on it.

Barbara Fecso's testimony supported three distinct defense propositions: the transaction could improve operations and lower prices; private suppliers would respond to regional price increases; and USDA could increase supply if necessary. The first concerns transaction benefits, the second private competitive constraints, and the third regulatory intervention. Fecso's experience with the Federal Sugar Program made her a persuasive industry witness, but she testified in her personal capacity, and USDA took no official position on the transaction. Evaluating a regulatory response requires evidence about its trigger, timing, magnitude, and ability to protect the affected customers. National tools can influence regional prices; their national scope alone does not answer the defense. The court's findings describe the program and her evidence, and its

concluding discussion explains the significance it assigned to USDA intervention (pp. 54-57, 92-96). The appeal, summarized below, rejected that legal rationale.

Judge Maryellen Noreika of the United States District Court for the District of Delaware rendered judgment for the merging parties and denied the DOJ's request for a permanent injunction. Read the judgment (p. 98). The outcome makes the case useful for examining how a prosecution is built and presented, while leaving room to disagree with parts of the court's analysis.

Preserving relief during an appeal. The DOJ indicated that it would appeal and sought an injunction pending appeal from the district court. Filing an appeal does not itself preserve an injunction preventing the parties from closing. Interim relief is important because consummation can complicate effective relief if the government later prevails. Civil Rule 62(d) authorizes an injunction while an appeal is pending, and Appellate Rule 8 ordinarily requires the applicant to seek relief first from the district court. Read Rule 62(d) (p. 196). The district court found that the DOJ had not shown a sufficient likelihood of success following the trial. It also rejected the DOJ's claim that closing would cause irreparable harm by making the transaction difficult to unwind, emphasizing the availability of post-closing divestiture. Its public interest analysis relied on anticipated efficiencies and lower prices, including Fecso's testimony. The defendants' account of the transaction's benefits thus mattered both to the merits litigation and to the request to prevent closing during the appeal. Read the district court's order denying the DOJ's motion (pp. 102-04).

Having filed its Notice of Appeal (NOA) and following the denial of its Rule 62(d) motion by the district court, the DOJ filed an emergency motion seeking an injunction pending appeal under Rule 8 of the Federal Rules of Appellate Procedure. Read the Notice of Appeal (pp. 99-101) and Rule 8 (p. 197). The motion also sought a short administrative injunction to preserve the status quo while the court considered the request for an injunction pending appeal. The substantive request involved likelihood of success on appeal, likely irreparable injury, harm to other parties, and the public interest. The DOJ's presentation of those factors is advocacy for interim relief, not a ruling that its merits arguments were correct. Read the discussion of the standards for an injunction pending appeal (pp. 112-13). Skim the remainder of the motion (pp. 106-11, 114-32). There is no need to read the opposition brief (pp. 133-61) and the DOJ's reply (pp. 162-72), but they are short and somewhat interesting. The Third Circuit's short interim order denied the requested relief and expedited the appeal; it did not supply the reasoned merits analysis found in the later appellate opinion. Read the interim order (pp. 173-74). The parties subsequently closed on November 28, 2022, while the appeal was pending. Read their letter reporting the closing (p. 175).

What the appeal resolved. The Third Circuit ultimately affirmed because the district court's rejection of the DOJ's product market was not clearly erroneous. Distributor competition and the unsupported aggregation of customer groups sustained that result; the court did not decide the geographic market issue. It also explained that the HMT is not the exclusive permissible means of defining a market. The appellate court rejected the district court's reliance on USDA intervention as a safeguard against antitrust harm: discretionary regulation and price supports do not create antitrust immunity. That error did not change the outcome because the product market ruling independently defeated the case. The litigation lesson is that winning a legal point on appeal cannot cure an independently sufficient failure of proof. The full appellate opinion

remains optional unless you are especially interested (pp. 176-94; product market discussion at pp. 184-92 and USDA discussion at pp. 192-94).

We will run class a little differently. While I have slides and will show some of them to get us started, I intend to spend most of the class discussing what the DOJ did wrong in the litigation and how the merging parties supported their competing account. The doctrinal distinctions above provide the foundation for that discussion; the class will emphasize using the theories, tools, and evidence to build a persuasive case.

Comparisons on geographic market definition. The remaining readings put *U.S. Sugar* in perspective by showing how different records support or undermine proposed geographic boundaries. The 2010 Horizontal Merger Guidelines distinguish supplier-location from customer-location markets. The 2023 Merger Guidelines retain that distinction and expressly separate supplier responses from demand-based market definition. Read the geographic market excerpts (2010 Guidelines, pp. 199-202; 2023 Guidelines, pp. 203-05). The 2010 framework was available at the time of the *U.S. Sugar* trial; the 2023 text supplies a subsequent comparison, not a standard the district court applied.

Sanford Health and *Advocate* illustrate the importance of identifying the actual purchaser and the competitive constraint. Insurers need provider networks that are attractive to employers and patients. In *Sanford Health*, the evidence showed that a plan lacking the relevant local physician services would not be marketable and that insurers would accept a hypothetical monopolist's price increase rather than omit them. In *Advocate*, the Seventh Circuit rejected the inference that patients who already traveled outside the area established that enough others would switch to defeat a price increase. Patient travel patterns and insurer substitution are related, but they are not interchangeable. Read the two excerpts as applications of geographic market definition to network bargaining (*Sanford Health*, pp. 206-07; *Advocate*, pp. 208-16).

Tronox provides a useful comparison to the geographic market dispute in *U.S. Sugar*. Substantial international trade did not preclude a North American customer-location market for chloride-process titanium dioxide. The FTC supported its market with regional pricing evidence, customer and supplier testimony, and analysis of the practical limits on importing or redirecting additional supply. Its economist, Nicholas Hill, also compared the critical loss from a 10% price increase with predicted losses. A 15.4% critical loss is a break-even threshold, not a prediction of how customers would respond. His estimates of predicted sales loss were below that threshold; for example, the elasticity-based estimate was approximately 4.5%. The conclusion therefore depended on evidence supporting predicted substitution as well as on the arithmetic. Read the *Tronox* excerpt (pp. 217-22). I hope you especially enjoy this passage since you should now know enough to understand the critical loss implementation of the hypothetical monopolist test. The opinion's reference to a "narrowest market principle" should not obscure the Guidelines' recognition that more than one market can satisfy the HMT.

JetBlue supplies a further distinction between national operations and the alternatives available to customers. Airlines organize networks nationally and can move aircraft among routes, but a flight between one origin and destination generally does not substitute for a flight between a different pair. The court accordingly used route markets while recognizing the industry's national features. Aircraft mobility is relevant to the likely competitive response; it does not by itself make all routes demand substitutes. Read the *JetBlue* excerpt and accompanying notes (pp. 223-27). The court's treatment of routes that Spirit had merely considered entering should

not be read as a general rule that Section 7 excludes potential competition. The accompanying notes describe later events as of 2024, including the termination of the merger agreement on March 4, 2024.

Enjoy the reading! Email me if you have any questions.

P.S. We will not have time in class to go through the background of the case, so I have posted the relevant portions of the class slides I would have used if we had the time. You do not need these if you read the opinion carefully, but I pass them along for whatever they are worth. These advance distribution class slides are separate from the supply-side switching class notes assigned above.