No. 71-873

In the Supreme Court of the United States

OCTOBER TERM, 1972

UNITED STATES OF AMERICA, APPELLANT

v.

FALSTAFF BREWING CORPORATION AND NARRAGANSETT BREWING COMPANY

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF RHODE ISLAND

REPLY BRIEF FOR THE UNITED STATES

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Falstaff misconceives the standard of proof required to establish that an acquisition's effect "may be substantially to lessen competition" within the meaning of Section 7 of the Clayton Act. Under its analysis the government apparently would have to show that Falstaff's management had affirmatively decided to enter the New England market, and then had changed its plans because it determined to acquire Narragansett; that small breweries which might form the basis for foothold entry were currently for sale on terms acceptable to Falstaff; and that as a result of its decision to enter by acquisition of a large market share, concentration in New England actually increased. Such requirements would make Section 7 virtually inapplicable to cases involving the elimination of potential competition.

The purpose of Section 7 was to stem a rising tide of concentration in American industry. Congress's concern with structural factors was based upon its belief that industry structure is the index of measurable competition. Apart from the use of criteria such as relative market shares, and concentration, it is, as Falstaff's expert testified, "very hard to measure if not impossible to measure the degree of competition among the firms" (App. 230). That is why this Court has in numerous decisions under Section 7 concluded that market structure—the total number of firms, their relative market shares, the extent of concentration among the leading firms, barriers to entry, and the influence of outside firms as potential competitors—is the standard by which a tendency toward the lessening of competition will be measured (U.S. Br., p. 16).

In applying Section 7 to this case, therefore, the government was required to demonstrate only that Falstaff's place in the structure of the New England market was that of a significant potential competitor; and that its self-elimination from that role by acquiring Narragansett's 20 percent market share, instead of entering as a new or foothold competitor, would probably lessen competition substantially. As explained in our main brief, the government made that showing.

a. *Falstaff as a potential competitor in New England.* To establish that Falstaff was a significant potential competitor in the New England market, the government showed, from objective evidence, that considering the concentrated structure of the New England market, Falstaff's financial capability to enter independently or by a foothold acquisition, its economic incentive to do so, and the reasonable prospects for making such an entry successful, there existed a basis for entry which would be reasonably acceptable to prudent management, if entry by acquisition were not available. (U.S. Br. p. 25.)

Whether in fact Falstaff's management would have entered is not the point. For the question is not what management would have done, but what it reasonably could have been expected to do. It is the latter factor that makes potential competition a significant influence upon market structure.

Under this practical criterion, the government met its burden. It showed the New England market was expanding, that Falstaff's business advisor (Little) had urged it to enter the Northeast *de novo* (and had warned of the antitrust risks of entering by a large acquisition, App. 557); that numerous small distributors were anxious to handle its product; that, according to its own expert, Falstaff could have earned a better rate of return on a new plant than it in fact has earned from the acquisition (App. 287-289);

that it had substantial experience in expanding small, faltering breweries into profitable operations; that it had a superior financial rating which would enable it to obtain financing; and that it had been a leader in developing its own distributor organization. All of these factors demonstrate that its independent or foothold entry could be considered a prudent business risk and that it thus was an influence on the market. Indeed, the small distributors who had written to it, and the two small breweries which invited it to acquire them, are strong evidence that even at their level Falstaff's role as a potential competitor was recognized.

Falstaff argues that the government, to show reasonable prospects for successful entry, must ascertain "the potential profit which Falstaff might have earned" by entering New England *de novo* or by a foothold entry (Br. 13-14). But its influence as a potential entrant could affect the pricing behavior of firms in the market, so that prices became stabilized below the level of profitability which would encourage it to enter. *United States* v. *Penn-Olin Co.*, 378 U.S. 158, 174. Insofar as the profit Falstaff might have earned by actual entry is concerned, proof of what might have been is always conjectural. All that can, or need, be proved is that a reasonable basis for successful entry exists. And this basis necessarily takes into account the fact that all marketing decisions involve some risk.

Falstaff's erroneous insistence upon precise proof of what might have been also permeates its contention that it could not have made a foothold acquisition in New England. It calls for proof of the terms on which such acquisitions might have been made (Br. 21-22). But again, Section 7, which concerns only probabilities, does not go so far. As we have shown (U.S. Br., p. 36), both Dawson's Brewery in New Bedford, Massachusetts, and Diamond Spring in Lawrence, Massachusetts, had made overtures to Falstaff (App. 324-325), and Falstaff had approached New York and New Jersey brewers (Piel's, Ballentine's,[1] Liebman's) with substantial New England sales (U.S. Br. 31). Even without such overtures, however, the smaller firms represented the same kind of candidates for lawful acquisition as the many other small breweries Falstaff had acquired and developed as it grew to its present size and strength. See *Kennecott Copper Corp.*, 3 Trade Reg. Rep. ¶ 19,619 (FTC), affirmed, C.A. 10 No. 71-1371 (September 15, 1972).

We do not question that Falstaff might not have found the acquisition of one of the smaller companies in the market to be as "attractive" (Br. 21-22) as the acquisition of Narragansett's strong market position and distributor organization. Anticompetitive acquisitions are attractive precisely because they are highly profitable. But it is the purpose of Section 7 to channel profit-making decisions into pro-competitive directions. Hence the comparative attractiveness of easy entry by acquisition against more difficult

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[1] Falstaff has now acquired certain Ballentine assets (U.S. Br. p. 10, n. 14).

entry by competition is not relevant where the latter is feasible under the criteria we have outlined.

b. *Competitive Effect.* Falstaff contends that the post acquisition evidence conclusively shows that its acquisition of Narragansett was not anticompetitive because prices in the market have remained constant, concentration has not increased and Narragansett-Falstaff has acquired no power over prices. It also argues that there has been no adverse competitive effect because, despite the acquisition, Narragansett's market share has decreased.

This argument misconceives the competitive issue. The anticompetitive effect of the acquisition is the loss of Falstaff's presence as an aggressive firm standing on the edge of the New England (and the Northeastern) market. What would have been gained, had Falstaff entered *de novo* or by a foothold acquisition, would have been a vigorous new competitor which, in its struggle to enlarge its market share, would have altered the structure of this concentrated market by introducing an additional and vigorous competitive factor. That struggle might even have resulted in lower prices.

Instead, concentration remained at the same levels, prices have not declined, and the structural influence of Falstaff as a potential competitor has been lost. Growth or shrinkage in Narragansett's market share thus sheds no light on whether the merger eliminated potential competition in the New England beer market.

CONCLUSION

The judgment of the district court should be reversed and the case remanded for the entry of an appropriate decree.

Respectfully submitted.

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