Class 16 slides

Unit 10: U.S. Sugar/Imperial Sugar

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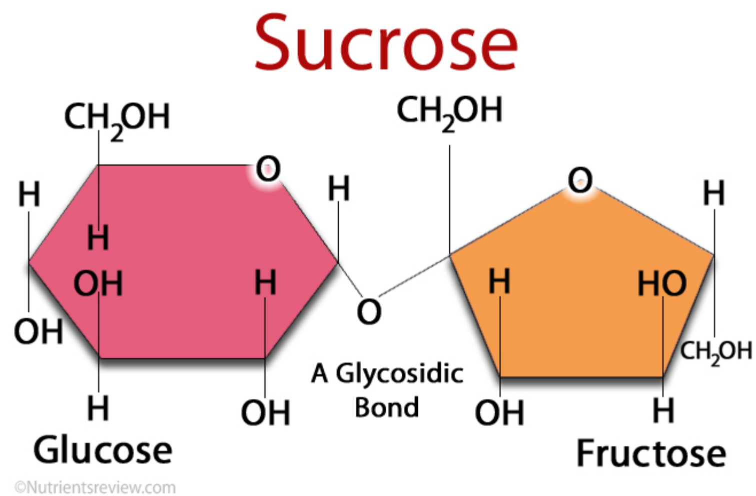
The Sugar Industry

The sugar industry

- Refined sugar
  - Food-grade sugar that is produced by refining sugar cane or processing sugar beets into sucrose (a combination of glucose and fructose)
  - Refined sugar produced from sugar beets is chemically identical to that produced from sugar cane
  - Types:
    - Granulated (99.5% sucrose—white in color)
    - Brown
    - Powdered
    - Liquid

Produced from additional processing of granulated sugar



Sugar production from sugar cane

Sugar cane

- Perennial grass containing about 14% sucrose
- Grown in Florida (51.9%), Louisiana (44.6%), and Texas (3.5%)
- Not imported—Value-to-weight ratio too low

Raw sugar

- Partially refined sugar processed from sugar cane
- Sugar mills close to the sugar cane plantations crush the cane and extract/partially refine sugar
- Primarily sucrose (96-99%) with some natural molasses
- Light brown in color
- Relatively inexpensive to transport
- Significant imports
- Can be consumed

Refined sugar

- Fully refined sugar processed from raw sugar
- Types:
  - Granulated (99.5% sucrose -- white in color)
  - Brown, powdered, liquid—produced from granulated
- Significant imports

Sugar production from sugar beets

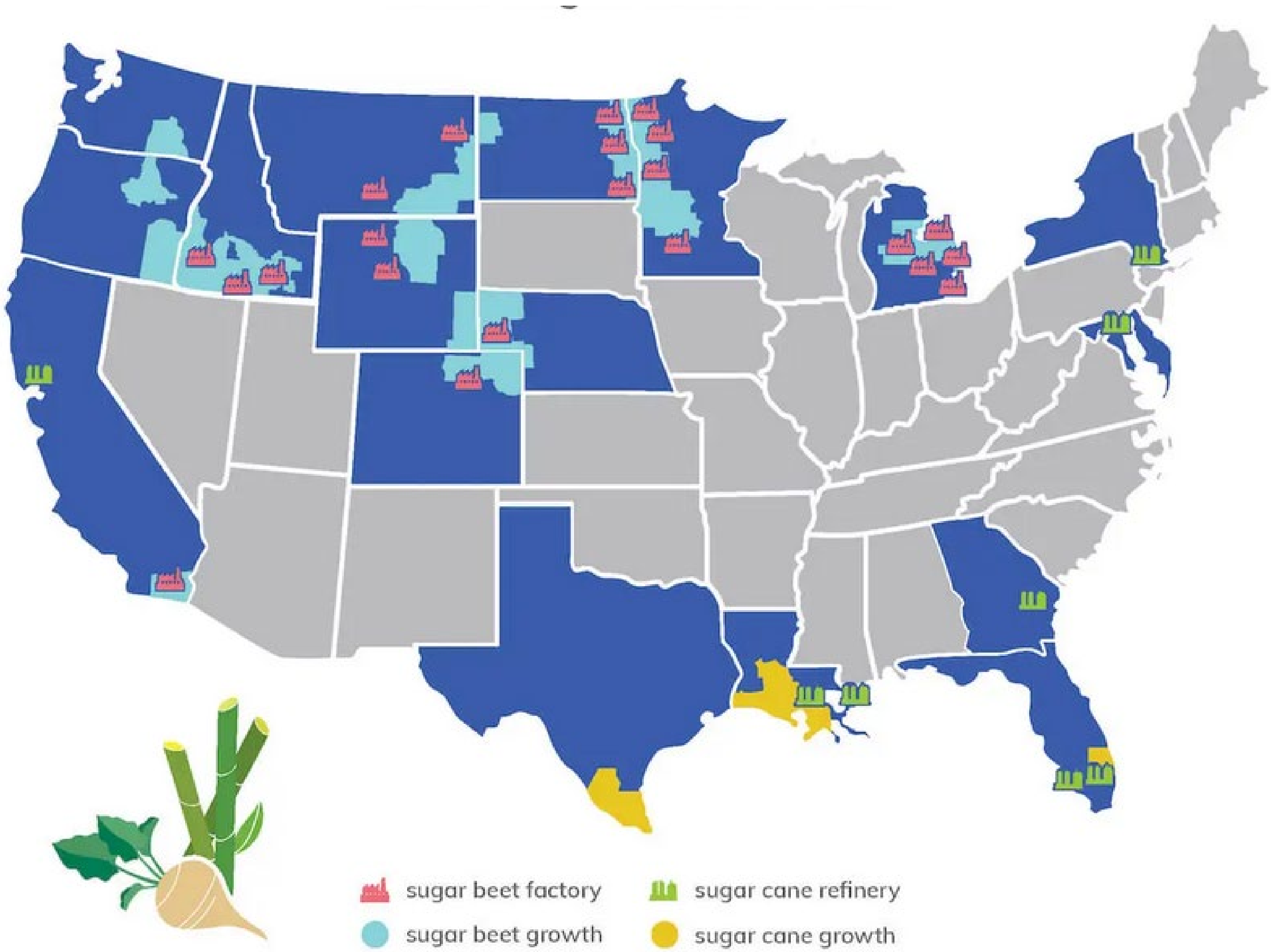
Sugar beets

- Root crop containing about 16% sucrose
- Grown in eleven states: California, Colorado, Idaho, Michigan, Minnesota, Montana, Nebraska, North Dakota, Oregon, Washington, and Wyoming

Refined sugar

- Fully refined sugar directly from sugar beets
- Chemically identical to sugar produced from sugar cane
- 99.5% sucrose (0.5% water)
- Seven U.S. sugar refiners
- White in color (without additives)
- Significant imports

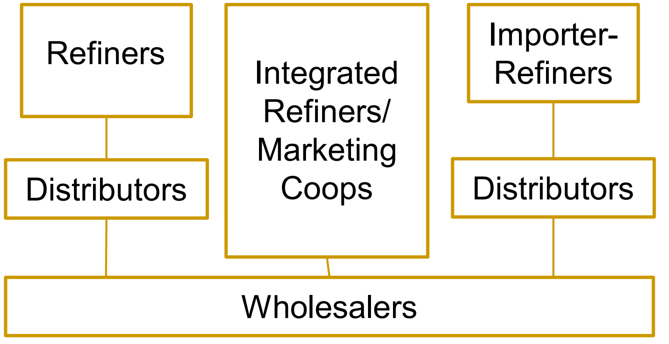
U.S. sugar production



Source: The Sugar Ass'n, U.S. Sugar Industry

Industry organization

- Production, distribution, and sale



- Distributors (including marketing coops)
  - Purchase refined sugar from refiners or importers
  - May repackage it or further process it into liquid, invert, brown, or powdered sugar
  - May offer nationwide shipping using rail transfer stations and their own trucking fleets
- Wholesaler purchasers
  - Most purchases done through a "Request for Proposal" (RFP)
    - Most RFPs are for delivered prices
  - Essentially, suppliers bid for wholesaler business through their responses to the RFPs

USDA Federal Sugar Program

- Sugar supply is largely regulated by the USDA

> The Federal Sugar Program, as run by the USDA, purports to balance somewhat competing government policies that impact the price of sugar - i.e., the Government's support of American sugar cane and sugar beet farmers by ensuring that there is a guaranteed floor price to be able to stay in business and the Government's interest in ensuring that sugar prices do not get too high for the many businesses (known as sugar "users") that buy sugar to use in their products.[1]

- The USDA controls the supply of sugar in the United States through—
  1. Marketing allotments for domestic sugar processors
     - Individually set for each processor
     - Caps the amount of sugar the processor is allowed to sell
  2. A system of tariff rate quotas (TRQs) on sugar imports and free trade agreements
     - Imports under the quota are charged a discounted duty rate
     - Imports over the quota are charged the full duty rate—essentially makes these imports unviable
     - → TRQ imports effectively constrain domestic prices
  3. Control over Mexican imports under the U.S. Mexico Suspension Agreements
  4. Since 2007, USDA has taken at least 30 actions to increase foreign sugar imports into the U.S. when it believed that additional supply was necessary

[1] Op. at 16.

The Deal

The deal

- U.S. Sugar to buy Imperial Sugar
  - Merger Agreement signed March 24, 2021
  - Purchase price: $315 million
    - Later reduced to $297 million
  - Asset purchase—Buying only assets, not stock
    - Imperial's Port Wentworth facility
    - Imperial's leasehold interest in a sugar transfer and liquification facility in Ludlow, KY
    - Four retail sugar brands:
      - Imperial Sugar
      - Dixie Crystals
      - White gold
      - Holly Sugar
  - Drop-dead date: September 24, 2022

The parties

- U.S. Sugar
  - Privately held Delaware corporation headquartered in Clewiston, FL
  - Owns and operates a cane mill and cane refinery in Clewiston
    - Refinery capacity: 850,000 tons annually—operates at maximum capacity
    - Produces only granulated and liquid sugar
      - Not brown or powdered sugar
    - Less than 7% nationwide refined sugar capacity
  - Vertically integrated in sugar cane growing
    - Plantations in South-Central Florida (200,000 acres)
    - Grows more sugar than U.S. Sugar can process
    - So sells sugar cane to third-party mills in Florida
  - Vertically integrated into distribution
    - USG owns United Sugars Corporation ("United") with three other sugar producers
      - United States Sugar (cane sugar)
      - American Crystal Sugar Company (beet sugar)
      - Minn-Dak Farmers Cooperative (beet sugar)
      - Wyoming Sugar Company, LLC (beet sugar)
    - United is a marketing cooperative that controls the pricing, marketing, and sale of all the sugar of its four members[1]
      - Sells sugar in 45 states

[1] Presumably, United is immune from the antitrust laws as an agricultural cooperative under the Capper-Volstead Act, 7 U.S.C. § 291.

The parties

- Imperial Sugar
  - Headquartered in Sugar Land, TX
    - Wholly-owned by Louis Dreyfus, a leading worldwide merchant and processor of agricultural goods headquartered in the Netherlands
  - Owns and operates cane sugar refinery in Port Wentworth, GA
    - Imperial Sugar's principal asset
      - Experienced a major explosion in 2008 that destroyed the plant—damaged part rebuilt in 2009
    - Capacity: _______
    - Produces granulated, brown, powdered, and liquid sugar
    - Sells refined sugar into more than 40 states, including Texas, Indiana, Pennsylvania, and Ohio out of Port Wentworth
  - Does not own any cane farming or milling assets—imports > 90% of raw sugar

Imperial's Port Wentworth sugar refinery

After 2008 explosion

Today

Deal benefits[1]

- Imperial's Port Wentworth current operations
  1. Input supply limitations
     - Import-based refiner—imports > 90% of its raw sugar
     - Still, can only run at about 75% of capacity due to lack of supply (sometimes only 60-65%)
     - Accounts for about 7% of nationwide sugar refining capacity
  2. Input cost limitations
     - Raw sugar comprises about 70-80% of the delivered price of Imperial's refined sugar
     - Has higher input costs than refineries vertically integrated into sugar cane or sugar beets
  3. Investment limitations
     - High-cost producer dependent on imports subject to tariffs
     - Some equipment from the 1940s
     - Uncertain financial future
     - Louis Dreyfus has limited investment to maintenance and safety/health/environmental
  4. Market position
     - Declining over the last several years
     - Principally a residual or back-up supplier
  5. Prospects of sale
     - Louis Dreyfus has been trying to sell Imperial for the last five years

[1] Taken from findings of fact in the opinion. Op. at 22-23.

Deal benefits

- Benefits of acquisition
  1. Mitigation of input supply limitations
     - U.S. Sugar grows more sugar cane than it can process and refine
     - U.S. Sugar will be able to provide between 84,000-168,000 short tons annually to Port Wentworth
  2. Production expansion
     - U.S. Sugar plans to expand Port Wentworth's annual production from 805,000 short tons to 875,000 short tons, an increase of 70,000 short tons or 8.7%[1]
     - U.S. Sugar will use "targeted expenditures" to increase the capacity utilization at Port Wentworth
  3. Transportation cost savings
     - Adding Port Wentworth to the United distribution network expected to save $8-12 million (annually?)
  4. Reliability of supply
     - Adding Port Wentworth to the United distribution network will increase reliability of supply to—
       - Premerger Port Wentworth customers
       - U.S. Sugar/United customers in the event of an adverse weather event in the Red River Valley or in Florida
  5. Port Wentworth's future absent the acquisition
     - "If the U.S. Sugar acquisition does not proceed, Imperial's CEO is 'quite worried' about Imperial's future prospects."

[1] The opinion gives the difference as 140 million pounds. Op. at 22. Some conversions are necessary. The opinion gives the before and after numbers in cwt (hundredweight, short, US), which equals 0.5 short tons. Converting cwt to short tons, the before and after production levels are 805,000 and 875,000, respectively (as given in the text), for a difference of 70,000 short tons. But each short ton equals 2000 pounds, so 70,000 short tons equals 140 million pounds.

DOJ complaint

- *Filed*: November 23, 2021
  - Seven months after the signing of the merger agreement
- *Claim*:
  - Acquisition would substantially lessen competition—
    - in the production and sale of refined sugar
    - to wholesale customers
    - In—
      1. the Southeastern United States, *and*
      2. Georgia

Relevant product market

Targeted customers

Relevant geographic markets

- *Prayer*: Permanent injunctive relief blocking the transaction

DOJ complaint

- A note on the DOJ's prima facie case of anticompetitive effect
  - The *PNB* presumption: Transaction treated largely as a 3-to-2 merger with a fringe[1]
    - Southeastern United States
      - Combined share: 46%
      - Delta: 800
      - Postmerger HHI: 2800
      - Postmerger 2FCR: 75%

From DOJ Post-Trial Brief

    - Georgia
      - Combined share: 54%
      - Delta: 1100
      - Postmerger HHI: 3100
      - Postmerger 2FCR: 75%

From DOJ Post-Trial Brief

[1] The third major player in the alleged markets was American Sugar Refining Company (ASR), also known as Domino Sugar. ASR has two cane sugar refineries: Chalmette, Louisiana (which sells in 44 states) and Okeelanta, Florida (which sales in ___ states [redacted in opinion]).

DOJ complaint

- A note on the DOJ's prima facie case of anticompetitive effect
  - A trick in deconstructing market share
    - In many opinions, the market shares of the merging parties are redacted
    - However, the opinion may report the combined market share and the associated HHI
    - Let *a* and *b* be the market shares of the merging companies
    - Then:

$$a + b = \text{combined share}$$
$$2ab = \text{delta}$$

    - These are two simultaneous equations in two unknowns, so you can solve for *a* and *b*
    - If you like, use a simultaneous equations calculator like [Symbolab]
  - Here:

			Solving:
Southeastern United States			
Combined share:	46%	$a + b = 46\%$	$a = 37.7\%$
Delta	800	$2ab = 800$	$b = 11.4\%$
Georgia			
Combined share:	54%	$a + b = 54$	$a = 40.7\%$
Delta:	1100	$2ab = 1100$	$b = 13.4\%$

DOJ complaint

- A note on the DOJ's prima facie case of anticompetitive effect
  - Dimensions of anticompetitive harm
    - Price
    - (Throwaway:) Reliability of supply
  - Auction unilateral effects
    - "The proposed transaction would eliminate head-to-head competition between United and Imperial in both relevant markets."
    - The idea
      - United and Imperial are the two lowest cost suppliers for some customers and the acquisition will eliminate their independence
      - Competition for these customers will be between the combined firm and the third-lowest-cost supplier, resulting in an anticompetitively higher winning bid price[1]

[1] We will develop this bidding theory of unilateral effects in the next class when we study Sysco/U.S. Foods.

DOJ complaint

- A note on the DOJ's prima facie case of anticompetitive effect
  - Coordinated effects

> "The proposed transaction would increase the incentive and ability of industry giants United and Domino to coordinate to raise prices and reduce quality."

- Premerger susceptibility
  - Refined sugar is a relatively homogeneous product
  - Sugars prices "relatively transparent" (from customers)/Competitors monitor each other's prices
  - Competitors can readily identify incumbent suppliers for each customer—makes it easy for coordinating firms from "poaching" each other's customers
  - Only three significant competitors in the two markets: USS/United, Domino, and Imperial
  - High barriers to entry/expansion
- Increased likelihood or effectiveness
  - Only two significant competitors would remain postmerger: USS/United and Domino
  - Transaction mores closely aligns the incentives of USS/United and Domino by increasing homogeneity across firms
    - Factors:
      - Domino is a large vertically integrated firm that imports some raw sugar
      - USS is somewhat smaller and imports no sugar/Imperial purchases some imported raw sugar
    - Creates more similarly sized firms
    - Creates a similar level of vertical integration [WDC: ???]

DOJ complaint

- A note on DOJ's response to anticipated downward pricing pressure defenses
  - Entry/expansion defense

    "Entry and expansion will not prevent the substantial harm threatened by this deal"

    - High barriers to building or expanding a refinery
    - High transportation costs limit the ability of outside refiners to increase shipments into the relevant markets
  - Efficiencies defense

    "There are no merger-specific efficiencies that outweigh the substantial harm threatened by this deal"

[1] Complaint ¶ 57.

DOJ complaint

- A note on the USDA Federal Sugar Program

> "USDA's sugar policy will not prevent the substantial harm threatened by this deal"

  - USDA does not run its programs to ensure competition in the sale of refined sugar to wholesalers
  - USDA programs permits "significant regional variations in the prices charged to customers due to differences in competitive conditions in each area"[1]

[1] Complaint ¶ 57.

DOJ complaint

- Request for relief
  1. Declaration that the acquisition would violate Section 7
  2. Permanently enjoining defendants from consummating the acquisition
  3. Award the United States the costs of its action
  4. Grant the United States such other relief as the Court deems just and proper

The trial

- Venue
  - Filed November 23, 2021
  - In the District of Delaware
- Judge Maryellen Noreika
  - Nominated by President Donald Trump
  - Sworn in: August 9, 2018
  - Reportedly considered by President Biden for the Federal Circuit
- Trial
  - Parties stipulated to a TRO—proceeded to trial on the merits
    - Court consolidated proceedings under Rule 65(a)(2)
  - Trial began on April 18, 2022 (four days)—5 months after the complaint was filed
    - 30 fact witnesses/2 expert witnesses
    - Exhibits: 24 (joint), 74 (plaintiffs), 31 (defendants)
  - Decision: Permanent injunction denied on Sept. 23, 2022
    - 9 months after complaint filed
  - Affirmed by the Third Circuit

Experts

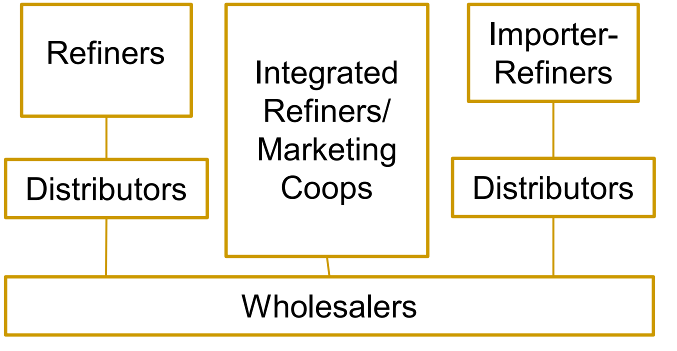
- DOJ: Dr. Dov Rothman
  - Managing principal at Analysis Group
  - Ph.D in business administration from the Haas School of Business, University of California, Berkeley
  - Joined Analysis Group in 2006
  - 2004-2006: Assistant Professor,
    Mailman School of Public Health, Columbia University
  - Testified in multiple antitrust cases
    - Including four merger cases for the government

- Merging parties: Dr. Nicholas Hill
  - Partner at Bates-White
  - Ph.D in economics, Johns Hopkins University
  - Joined Bates-white in 2017
  - Prior 12 years as a government antitrust economist
    - 2014-2017: ATD Assistant section chief
    - 2013-2014: FTC staff economist
    - 2006-2013: ATD staff economist
  - Testified in numerous antitrust cases

Relevant product market

- DOJ case-in-chief:
  - *Product type*: Refined sugar
    - Not distinguishing from sugar produced from cane or beets
    - Not contested by the merging parties
  - Market participants:
    - Includes refiners, marketing coops with refiner members, and importers

      DOJ post-trial brief and court opinion could be clearer here
      - *Query*: How to assign market shares when a marketing cooperative has multiple refiner members?
    - Excludes independent distributors
      - "The proper focus for this case is competitors that produce and sell refined sugar, and not distributors that resell sugar that they have purchased from refiners."[1]
      - *Argument*: Independent distributors must obtain their refined sugar from refiners, and the refiners can tacitly coordinate to limit the ability of these independent distributors to compete through decision on pricing and supply
    - Basic idea
      - Complaints focuses on the control of refiners of wholesale prices
      - Looks to an anticompetitive effect on sales to grocery stores, distributors, food and beverage manufacturers and other wholesale customers



[1] Plaintiff United States of America's Post-Trial Brief 15 (May 6, 2022).

Relevant product market

- DOJ allegations:
  - Market participants:
    - Excludes independent distributors—From DOJ's Post-Trial Brief:

> Distributors depend on refiners to obtain refined sugar and need to add a margin on top of the price that they pay for that refined sugar to stay profitable. As a result, distributors do not constrain refiners, but instead serve smaller customers (e.g., customers who need less than a truckload of sugar), fill gaps in larger customers' annual sugar purchases, or provide additional products or services not offered by the refiners. Defendants' own ordinary-course documents characterize distributors as customers and do not assign them market shares. Refiners partner with distributors when it suits them, and they disintermediate distributors and sell directly to end-use customers when it does not. Tellingly, even Defendants do not argue that distributors should be assigned market shares for all of their refined sugar sales in the relevant markets. In their closing argument, Defendants "admit[ted] there are certainly instances where distributors are not acting as a competitive constraint." Similarly, Dr. Hill conceded that at least some sales by distributors should be attributed back to the refiners who produced the sugar.[1]

    - There is judicial support for the proposition that distributors who simply resell products purchased from primary suppliers should be excluded from the relevant market containing the primary suppliers
      - Excluding distributors should depend on the distributors obtaining all (or close to all) of their products from primary suppliers in the putative "collusive group"
      - It needs to modified if distributors are obtaining a significant portion of their products from firms outside the collusive group

[1] Plaintiff United States of America's Post-Trial Brief 18-19 (May 6, 2022) (record citations omitted)

Relevant product market—Problem 1

- *Court*: The DOJ failed to make out a prima facie case that independent distributors should be excluded from the relevant market
  - *Fundamental conceptual issue*: Consider two scenarios—
    1. A sugar beet processor that does not sell into the DOJ's market sells to an independent distributor that does sell into the DOJ's market. Neither company is a participant in the DOJ's market
    2. Same sugar beet processor and distributor, but they are in an agricultural coop. The processor/coop are now a participant in the market.

    Court:
    - Makes no economic sense to exclude the distributor in the first scenario but include it in the second scenario
    - Ignores the "market realities" of the competition the distributor brings to the relevant market in the first scenario
  - Evidence shows that distributors compete against refiners
    - Customers do not care if they purchase from a refiner, a coop, or an independent distributor
    - Distributors sell large volumes of sugar into the southeastern United States
    - Numerous examples of distributors taking significant business away from refiners or refiner/coops
    - Distributors are not "controlled" by refiners from whom they purchase
      - Purchase from many sources (including imports of refined sugar)
      - Successfully compete against refiners that supply them
      - Refiners view distributors as competitors

Relevant product market—Problem 1

- *Court*: The DOJ failed to make out a prima facie case that distributors should be excluded from the relevant market
  - Conclusion:

> Because a division of the refined sugar market into "refiner or cooperative sold" refined sugar and "distributor sold" refined sugar would be inconsistent with the commercial realities of the industry, the Court must reject the Government's proposed product market. **And as the Government admits that it does not have evidence to prove its case if distributors are included in the product market, and there is no alternative product market offered, the Government cannot prevail in this case.**[1]

  - WDC:
    - Did defendants show that if distributors were included in the DOJ's alleged markets, the *PNB* presumption would not be triggered?
    - Or did the DOJ simply did not do the analysis to show that it would be triggered?

[1] Op. at 47.

Relevant product market—Problem 2

- *Court*: The DOJ failed to make out a prima facie case that industrial and retail wholesale customers should be included in the same market
  - The DOJ included both types of customers in its alleged markets
  - BUT—
    - Suppliers have separate sales teams for industrial and retail customers
    - Different suppliers can sell significantly different percentage sales to industrial and retail customers
    - Failure of proof in making out the prima facie case

> "At trial, the Government offered no testimony or documentary evidence from or about non-industrial customers to show that they are similarly situated to industrial customers such that all should be grouped together as 'wholesale customers' in the relevant product market."[1]

  - WDC:
    - Presumably, the defendants put this question into issue by introducing evidence of significant differences between industrial and retail wholesale customers
    - But it is strange that the court did not continue its analysis to show that separating the two customer types mattered to the conclusion of the competitive analysis
    - It is unlikely that the court would reject the DOJ's market definition on this ground alone, but it undoubtedly increased the court's confidence that the DOJ's product market definition was wrong

[1] Op. at 33.

Relevant geographic market

- DOJ allegations:
  - Two relevant geographic markets—
    1. The Southeastern United States
       - Alabama, Delaware, District of Columbia, Florida, Georgia, Kentucky, Maryland, Mississippi, North Carolina, South Carolina, Tennessee, Virginia, and West Virginia
       - Defined by the U.S. Census Bureau as the East South Central and South Atlantic
    2. “Georgia Plus”: Georgia plus five bordering states
       - Alabama, Georgia, Florida, South Carolina, North Carolina, and Tennessee
  - Defined by wholesale customer location
    - Wholesale customers purchase through RFPs for delivered price supply contracts
    - Wholesale customers do not engage in arbitrage—they use what they purchase
    - This allows suppliers to charge customers different prices based on their location depending on:
      - The cost of transportation from the refinery to the customer, *and*
      - The number and significance of other suppliers that can reasonably supply the customer
  - Economic support
    - Rothman’s application of the HMT

Relevant geographic market

- DOJ allegations:
  - Boundaries determined by high transportation costs of refined sugar:

> Transportation costs can add thousands of dollars to the total cost of a delivery, and the need to ship refined sugar even a few hundred additional miles can yield a substantially higher total price for the customer. **Based on data from United, shipping refined sugar an additional 500 miles by truck would increase the price of delivered sugar by over 10 percent. Making the same shipment entirely via rail, which is often impossible, would increase the price of delivered sugar by more than five percent.** Because of these transportation costs, wholesale customers in the Southeast rely heavily on producers that have large refineries located nearby. United has an advantage in this region through its ability to sell sugar from U.S. Sugar's refinery in Florida, as well as from other United members' refineries. Imperial is also well positioned to serve customers in the Southeast from its refinery in Savannah, Georgia.
>
> . . .
>
> [T]he cost to transport refined sugar limits the geographic reach from which a customer can cost-effectively buy refined sugar.[1]

[1] Complaint ¶¶ 4, 30.

Relevant geographic market

- Southeastern geographic market

Imperial refinery
(Port Wentworth, GA)

Florida Crystals (Domino) refinery
(Okeelanta, FL)

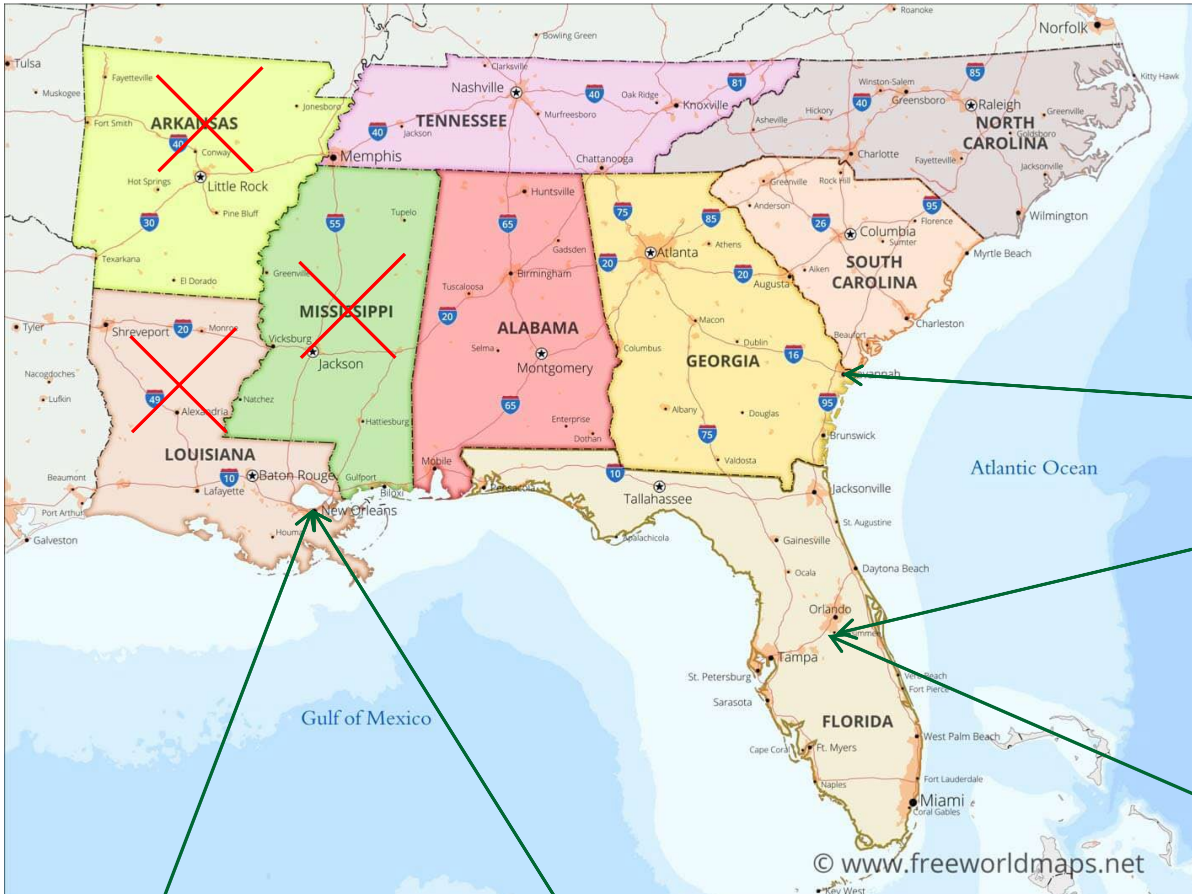
USS refinery
(Clewiston, FL)

LSR refinery
(Gramercy, LA)

Domino refinery
(Chalmette, LA)

Relevant geographic market

- Georgia plus five bordering states



Imperial refinery
(Port Wentworth, GA)

Florida Crystals (Domino) refinery
(Okeelanta, FL)

USS refinery
(Clewiston, FL)

LSR refinery
(Gramercy, LA)

Domino refinery
(Chalmette, LA)

Relevant geographic market

- *Court*: DOJ failed to make out a prima facie case that either of the alleged relevant geographic markets were proper markets in which to analyze the acquisition
  - Rothman did no independent analysis to determine whether these were proper candidate markets in which to begin the market definition analysis
    - The staff apparently defined the markets; Rothman just applied the HMT
    - Rothman cites no documents or the USDA that groups the states together in the alleged "Southeast" market and only one document for the "Georgia Plus" market
  - Shipments across alleged market boundaries
    - Customers in the alleged markets purchase and receive refined sugar—in large quantities—from many locations and suppliers outside of each market (citing numerous examples)
      - Many of these out-of-market suppliers have additional supply that could be sent into the market
    - Customers within the alleged markets also have the ability to pick up sugar at locations outside of the alleged markets
      - 30-35% of customers pick up sugar at their supplier
      - 3% of customers pick up sugar at a supplier location outside of the alleged geographic markets and transport the sugar into the market
    - Some suppliers outside of the alleged markets are expanding capacity and targeting sales in the alleged "Southeast" market
      - Especially true of suppliers located in Louisiana (e.g., LSR/Cargill)

Relevant geographic market

Source: The Sugar Ass'n, [U.S. Sugar Industry]

Relevant geographic market

- *Court*: The DOJ failed to make out a prima facie case that distributors should be excluded from the relevant market
  - WDC: More fundamentally, the DOJ improperly applied the HMT
    - The DOJ defined its markets by reference to customer locations
      - That is appropriate provided that the market participants are properly identified and their market shares properly assessed
    - The principal—if not only—economic support for the DOJ's alleged markets was the hypothetical monopolist test: Rothman apparently testified that—
      - Any product grouping that satisfies the HMT is a relevant market in which to analyze the transaction
      - A competitive problem in any one HMT-market is sufficient for the transaction to be anticompetitive in an economic sense
        - As an expert economist, Rothman could not testify whether the transaction would violate Section 7
    - In applying the hypothetical monopolist test, the DOJ apparently fixed the market shares at current sales and failed to take into account supply responses of firms outside of the market in assigning market shares to a price increase only within the relevant market[1]
      - Almost surely, the out-of-market supply-side responses would have eliminated the profitability of the price increase in both relevant markets

[1] For background, see the Market Definition class notes at slides 27-36.

PNB presumption

- Not addressed in opinion since DOJ failed to make out its prima facie case on market definition
  - However, the court almost surely was influenced by the failure of the DOJ's market shares to make economic sense
    - Failed to account to distributors as market participants and assign them shares
    - Failed to account for out-of-market suppliers who would increase shipments into the alleged market in response to an in-market SSNIP
    - Failed to account for out-of-market suppliers that did not ship refined sugar into the alleged markets today but would ship tomorrow in the event of an in-market SSNIP
    - Failed to account for planned capacity expansions and increased shipments into the alleged markets
  - All these factors would influence the state of competition in the alleged markets but are not captured by the market shares the DOJ sought to use to predicate the *PNB* presumption

The USDA as a competitive constraint

- DOJ:
  - USDA programs not designed or used to protect sugar markets from an anticompetitive effect arising from a merger
    - Appears to be an unsupported assertion
    - USDA did not testify at the trial—has no official position on the competitive effect of the acquisition
    - Does not appear to be any supporting testimony from anyone else

The USDA as a competitive constraint

- The merging parties:
  - The USDA has tools to ensure continued competition in the market postmerger in the event the transaction could affect sugar prices
    - Presented testimony by Dr. Barbara Fecso
      - Ph.D economist who worked at USDA for almost 30 years
      - Worked with the Federal Sugar Program for almost 20 years
      - Spoken with parties and learned of their postmerger plans
    - Fecso testimony:
      - Transaction unlikely to lead to higher prices
      - Instead, if claimed efficiencies are achieved, prices are likely to go down
      - Even if prices increased, supply would flow in from outside the market to bring prices back down
      - Failing that, USDA could "respond appropriately" (with support in the record)

> For example, in December 2021, the USDA increased the overall domestic allotment quantity and reassigned allotments to increase supply, doing so specifically to address "high sugar prices."[1]

    - *Query*: Was Fecso qualified as an expert witness under Rule 702?
      - Court did not say, but since offered opinions she should have been
      - UNLESS she somehow qualified as an "lay" expert under Rule 701

[1] Op. at 18.

The USDA as a competitive constraint

- Court:
  - Agreed with merging parties that the USDA has the tools to protect against any anticompetitive effect arising from the transaction
    - Found Dr. Fecso's testimony persuasive even though testifying in her personal capacity

> There is no one else at USDA that has a longer tenure working on the Federal Sugar Program or in making recommendations to the undersecretaries for the Federal Sugar Program. **The Court found Dr. Fecso to be an exceptionally knowledgeable and particularly credible witness.**[1]

    - Influence by the DOJ's decision not to offer USDA documents or testimony or even have Dr. Rothman talk to USDA officials:

> It is noteworthy that the Government did not offer any documentary or testimonial evidence from USDA as to its view of the anticipated effects of U.S. Sugar's acquisition of Imperial. In essence, the Government decided to shield USDA officials from having to answer questions about the interplay between free market competition and the Federal Sugar Program.[2]

[1] Op. at 56. [2] *Id*. at 55.

Lessons

- Why the DOJ lost
  1. Picked the wrong economist
     - Interestingly, the analytical portion of the opinion starts by slamming the DOJ's economist:
       - "Dr. Rothman's analysis in this case as flawed and largely unpersuasive."[1]
       - "Although the Court is not wholesale excluding Dr. Rothman from offering an economics opinion, his credentials and experience appear to be lacking, especially when compared to Dr. Nicholas Hill, Defendants' economic expert, who the Court found to be particularly credible."[2]
         - *Query*: Why didn't the court exclude Rothman's expert testimony as unreliable under Rule 702?
     - Do not use an economist whose testimony has been soundly rejected by multiple courts
       - Or even one court (if good alternatives exist—which they almost surely will)
       - Once an economist has been found flawed and unpersuasive by one court, subsequent courts will find it easier to find the expert unpersuasive

[1] Op. at 24.
[2] *Id*.

Lessons

- Why the DOJ lost
  2. The DOJ's alleged geographic markets did not comport with the "commercial realities"
     - Make the case for the market definition first using documents and testimony from business participants that support the alleged markets
       - Use the HMT as confirmation, not as the primary evidence
       - Especially important if the merging firms will present documents and testimony from business participants that contradict the alleged market as contrary to the commercial realities
     - Use your economist properly
       - The economist should develop an independent analysis of the relevant markets
         - Should not take the markets proposed by the staff as a starting point
       - Should start with an economic analysis of documents and deposition testimony
       - Support with a separate economic analysis of customer substitutability and supply-side switching
         - Find powerful anecdotes to illustrate conclusions
       - Finally, confirm with the HMT

Lessons

- Why the DOJ lost
  3. The DOJ's alleged product markets did not comport with the "commercial realities"
     a. The DOJ failed to include all firms that exert pricing pressure as market participants
        - If there is substantial business evidence is that a firm is a competitor in the market, then need compelling contrary evidence to reject that firm as a market participant
          - Here, multiple witnesses representing suppliers and distributors testified that independent sugar distributors competed with other sugar suppliers in selling refined sugar to customers
          - Yet the DOJ rejected independent distributors as market participants
     b. The DOJ failed to distinguish between refined sugar sales to industrial customers and sales to retail customers
        - Substantial testimony that the two types have significantly different needs and some major sellers (including United) have separate sales teams for each channel
        - Participation in each channel may differ considerably by seller
          - 90% of United sales into industrial, whereas only 50% of Domino's sales are industrial
          - *Failure of proof*: Court found the DOJ failed to offer testimony or documentary evidence to show that the two channels should be group together

Lessons

- Why the DOJ lost
  5. The DOJ's proffered market shares did not make economic sense
     - Not in the opinion, but probably an important factor in the outcome
     - The DOJ's market shares did not account for likely significant out-of-market supply-side responses to a in-market price increase, undermining confidence that the shares could be used to predicate the *PNB* presumption
  6. Failed to disprove the merging parties' claimed efficiencies
     - The opinion did not address the DOJ's challenge to the parties' claimed efficiencies, but the findings of fact make equally clear that efficiencies were accepted by and important to the judge
     - If the merging parties have a compelling efficiencies story to tell and persuasive witnesses to tell it, need equally compelling evidence to show that the claimed efficiencies are suspect and should not be considered
       - In this situation, a challenge only on verifiability or merger-specificity is increasing unlikely to work
       - Need a business witness or expert to disprove efficiencies
     - If the efficiencies cannot be disproved altogether, then some analysis is necessary to show that the transaction will be anticompetitive even in the presence of the efficiencies

Lessons

- Why the DOJ lost (con't)

6. Failed to disprove the merging parties' claimed efficiencies
   - The opinion did not address the DOJ's challenge to the parties' claimed efficiencies, but the findings of fact make equally clear that efficiencies were accepted by and important to the judge
   - If the merging parties have a compelling efficiencies story to tell and persuasive witnesses to tell it, need equally compelling evidence to show that the claimed efficiencies are suspect and should not be considered
     - In this situation, a challenge only on verifiability or merger-specificity is increasing unlikely to work
     - Need a business witness or expert to disprove efficiencies
   - If the efficiencies cannot be disproved altogether, then some analysis is necessary to show that the transaction will be anticompetitive even in the presence of the efficiencies
7. Failed to rebut Dr. Fesco
   - Needed some expert to testify that the tools the USDA has operate nationally and not regionally
   - Needed some expert to testify that the USDA—
     - does not monitor or care about regional price differences, *and*
     - would not take action to lower prices by increasing TRQs or reallocating processor allotments

Lessons

- Why the merging parties won
  1. The merging parties had a compelling story to tell and persuasive witnesses to tell it
     - A compelling efficiencies is critical to capturing the "heart" of the judge—a critical step in prevailing in the case
       - A compelling efficiencies story means that there is a consumer welfare loss if the court erroneously blocks a merger that is in fact not anticompetitive
       - Makes the court much more cautious in ruling for the plaintiffs
     - Focus on "easily" proved efficiencies—
       - Output expansion
         - Here, investment to expand plant capacity and new sources of raw sugar to fill plant to capacity
       - Input cost reduction
         - Here, shifting to low-cost internal supply of raw sugar and away from high-cost imports
  2. Successfully rebutted the DOJ's alleged geographic market definition
     - Substantial evidence in documents and business testimony of a significant out-of-market supplier response to a price increase
       - Evidence that out-of-market suppliers ship significant quantities into—and even across—the alleged markets today at prevailing prices
       - Evidence that out-of-market suppliers have significant (uncommitted) quantities available to ship into the alleged markets if reallocating shipments would increase profits
       - Evidence that out-of-market suppliers would respond to a SSNIP in the alleged market by shipping additional quantities into the market
       - Strong economic testimony of arbitrage that caused in-market and out-of-market prices to highly correlated (does not appear in opinion)

Lessons

- Why the merging parties won
  3. Successfully rebutted the DOJ's exclusion of distributors as market participants
     - Substantial evidence in documents and business testimony that distributors competed with—and were not controlled by—their refined sugar suppliers
       - Multiple examples of winning significant bids against suppliers
       - Evidence that suppliers considered distributors as competitors
       - Story as to why distributors could compete against suppliers
       - Strong supporting expert economic testimony
  4. Used the right economist
     - Experienced, with a great track record
     - Reputation for independence and thoroughness
     - Helpful that Hill had significant government experienced in merger analysis
  5. Had a very experienced and credible industry "expert" testifying in support of transaction
     - Transaction likely to lower prices if claimed efficiencies are achieved
     - Even if the combined firm could increase prices, USDA has the tools to control price levels