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# Not for Import: Why the EU Should not Adopt the American Efficiency Defense for Analyzing Mergers and Joint Ventures

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# NOT FOR IMPORT: WHY THE EU SHOULD NOT ADOPT THE AMERICAN EFFICIENCY DEFENSE FOR ANALYZING MERGERS AND JOINT VENTURES

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> "To admit an economies defense that proceeds by measurement would force us to an unacceptably narrow horizon. Economists, like other people, will measure what is susceptible of measurement and will tend to forget what is not, though what is forgotten may be far more important than what is measured."
>
> Robert Bork[1]
>
> "The measurement of efficiency. . .[is] an intractable subject for litigation."
>
> Richard Posner[2]

The avalanche of mergers and joint ventures with international dimensions that occurred in the nineties[3] has focused attention on the possibility of convergence or harmonization of the antitrust standards applied by different nations. As of 1998, over eighty nations had adopted some form of competition law, and dozens of other countries had competition statutes on the drawing board.[4] Multinational review of mergers and joint ventures has

* Professor of Law, Saint Louis University School of Law. Thanks to Professor Joël Mońeger, Universite d'Orleans, for his helpful insights.

1. ROBERT H. BORK, THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF 127 (1978).

2. RICHARD POSNER, ANTITRUST LAW: AN ECONOMIC PERSPECTIVE 112 (1976).

3. A large percentage of mergers reviewed by American enforcement agencies have involved competitive effects beyond American borders. In fiscal year 1998, thirteen of the twenty-eight merger enforcement actions undertaken by the Federal Trade Commission resulted in formal notifications to foreign governments, and of those six involved substantial discussions with foreign authorities also reviewing the mergers. In fiscal year 1999, twenty-one of thirty-eight merger investigations reaching the second requests stage involved notifications to foreign governments, of which twelve involved "substantial discussions" with foreign authorities. Richard G. Parker, *Global Merger Enforcement,* remarks at the International Bar Association, (Sept. 28, 1999).

4. A. DOUGLAS MELAMED, United States Dep't of Justice, ANTITRUST ENFORCEMENT IN A GLOBAL ECONOMY (1998).

become commonplace, and arrangements for sharing information, cooperating at the investigative stages, and in some instances, deferring to the judgment of sister enforcement agencies, have also developed.[5] Yet the goal of convergence on substantive standards in the form of an international competition code faces seemingly insurmountable hurdles rooted in political, cultural and philosophical factors.[6] At the same time, there is an unmistakable evolutionary process by which national authorities have learned from each others' experiences and that have caused substantive standards to move to some extent toward convergence.

Mergers and joint ventures involving large multinational corporations have garnered the most attention and the law applied by the world's most prominent enforcers (the American Department of Justice and Federal Trade Commission and the Commission of the European Union) has shown a surprising degree of consistency. This has resulted on numerous occasions in close cooperation, sharing of information and agreement on remedy between these agencies. For example, in the ABB/Elsag-Bailey merger, the EU and the FTC were able to reach speedy agreement on the dimensions of the market affected by the merger (a worldwide market for gas chromatography) and to find common ground on an appropriate divestiture.[7] Likewise, in the mammoth WorldCom/MCI merger, the Justice Department and the EU Commission closely cooperated, reaching the same conclusion on the competitive problems posed by the merger and agreeing to terms of a proposed divestiture of MCI's

5. Probably the most important form of cooperation occurs through cooperation between individual antitrust authorities in different nations. These arrangements are facilitated by bi-lateral agreements between nations or authorities that provide for notification of investigations affecting the other nation's interests and cooperation in the evidence gathering process. *See, e.g.*, Agreement Between the Government of the United States of America and the European Community Regarding the Application of their Competition Laws, Sept. 23, 1991, *reprinted in* 4 Trade Reg. Rpt. (CCH) ¶ 13,504, and OJ L 95/45 (Apr. 27, 1995), corrected at OJ L 131/38 (15 June 1995). Nations have also reached "positive comity" agreements that provide for formal or informal requests by a nation that another investigate a matter under its antitrust laws. *See* Agreement between the Government of the United States of America and the European Communities regarding the application of positive comity principles in the enforcement of their competition laws, June 4, 1998, *reprinted in* 4 Trade Reg. Rpt. (CCH) ¶ 13,504A; OJ L 173/26 (18 June 1998).

6. Commissioner Karel Von Miert of the Commission of the European Union proposed that the World Trade Organization members should agree to enact antitrust laws with "common principles or rules on anticompetitive practices with an international dimension and develop cooperation instruments and agree to binding arbitration arrangements to assure compliance. *See* MELAMED, *supra* note 4. For the negative American response to that proposal see *id.*; Joel Klein, *No Monopoly on Antitrust*, FINANCIAL TIMES, Feb. 13, 1998.

7. ABB/Elsag-Bailey, Case No. IV/M.139, European Commission decision of 16 Dec. 1998; In the Matter of Abb Ab and Abb Ag, FTC Docket No. C-1867, 64 F.R. 3130. *See* Parker, *Global Merger Enforcement*, *supra* note 3.

internet infrastructure assets.[8] On the other hand, in a few notable cases, EU and American authorities took decidedly different positions. Most prominent was the FTC's decision not to challenge Boeing's acquisition of McDonnell-Douglas while the EU found that the merger would have anticompetitive effects and insisted upon certain changes in Boeing's exclusive contracting practices as a condition of approving the merger.[9] Likewise, in the Ciba-Geigy/Sandoz merger, the FTC required divestiture based on a relevant market for gene therapy products and innovation which it believed was adversely affected by the merger, while the European Union Commission decided not to seek similar relief.[10]

The proper role for efficiency analysis in antitrust evaluations of mergers and joint ventures figured prominently in American antitrust policy in the 1990s. In a series of guidelines and policy statements, the federal enforcement agencies attempted to clarify the role efficiencies should play when evaluating mergers and joint ventures. In so doing, they have inadvertently opened the door for a full scale weighing of efficiencies at both the prosecutorial and judicial levels. Defendants now regularly assert an efficiency defense in litigation and, though none have been outcome-determinative as yet, several courts have undertaken to weigh efficiencies in analyzing mergers.[11] With EU antitrust enforcement evolving from a regime concerned with preserving open markets to one more focused on competitive analysis, it would come as no surprise if the EU enforcers likewise moved toward explicit weighing of efficiencies.[12]

All this would be fine if there were a working consensus on such fundamental questions as what kind of efficiencies should be recognized, whether there were reasonably accurate measurement of harms and efficiency benefits, and whether balancing of the two were feasible. This essay will argue that such is decidedly not the case. It will further contend that transplanting the emerging American approach to Europe will heighten uncertainty in the review of transnational mergers and perhaps invite nationalism and industrial

8. *See* MELAMED, *supra* note 4.

9. Boeing/McDonnell-Douglas, Case No. IV/M. 877, European Commission decision of 30 July 1997, O.J. L336/16 (Dec. 8, 1997); The Boeing Co., et al., Joint Statement Closing Investigation of Proposed Merger and Separate Statement of Commissioner Mary L. Azcuenaga, FTC File No. 971-0051 (July 1, 1997), *reprinted in* 5 Trad. Reg. Rep. (CCH) ¶ 24,295.

10. Ciba-Geigy, Ltd., et al., Consent Order Issued (Mar. 24, 1997) *reprinted* in 5 Trad. Reg. Rep. (CCH) ¶ 24,182. Ciba-Geigy/Sandoz, Case No. IV/M. 737, Commission Decision of 17 July 1996, OJ L 201 (July 29, 1997).

11. *See, e.g.*, FTC v. Staples, Inc., 970 F. Supp. 1066 (D. D.C. 1997); FTC v. Cardinal Health, Inc., 12 F. Supp.2d 34 (D. D.C. 1998). *See infra* note 84 and accompanying text.

12. *See* Peter D. Camesasca, *The Explicit Efficiency Defense in Merger Control: Does It Make A Difference?*, 1999 E.C.L. REV. 14 (1999) (describing the "implicit efficiency defense" in merger assessments performed by the EU's Merger Task Force and discussing the possibility of heightened scrutiny of efficiencies in the future).

policy to intrude upon these reviews. Finally, the essay offers a few discouraging words and caveats about the capacity of the litigation process to handle complex economic inquiries while also warning of the regulatory black hole awaiting those who undertake efficiency balancing at the prosecutorial level.

## I. THE EMERGING AMERICAN ANTITRUST EFFICIENCY ANALYSIS

Following up on a commitment made during his confirmation hearings and pursuing a topic of long-standing academic interest, FTC Chairman Robert Pitofsky initiated in October 1995 a series of hearings concerning the status of antitrust law and its role in the changing global economic environment. One of the issues posed by the hearings was whether "American antitrust enforcement [has] paid sufficient attention to claims of efficiency." Following extensive testimony on this subject, the FTC staff issued, in June 1996, a report entitled *Anticipating The 21st Century: Competition Policy in the New High-Tech Global Marketplace*.[13] Responding to some of the suggestions contained in the FTC Staff Report, but not adopting them wholesale, the FTC and the Justice Department revised the discussion of efficiencies in their joint guidelines governing horizontal mergers in 1997[14] and more recently issued new "Collaboration Guidelines" on the subject of the agencies' enforcement policies respecting joint ventures.[15] Though the changes proposed by the FTC Staff Report and Collaboration Guidelines are neither new nor radical, they evidence a continuation in the law's drift toward a more comprehensive and "dynamic" look at efficiencies in merger and joint venture investigations. With the likely diffusion of the federal enforcement agencies' methodology into litigation and judicial decision-making, these changes, if adopted, are apt to have an important impact on merger jurisprudence. This section briefly traces the emerging American approach to analyzing efficiencies arising out of mergers and joint ventures.

### *A. The Revised Merger Guidelines*

Given the rather dismal record of the federal agencies on such issues as geographic market and barriers to entry in litigated merger cases, one might be a bit surprised that the FTC would voluntarily leap into the efficiencies quagmire. Indeed, having lost more merger cases in federal court than they

13. FEDERAL TRADE COMM'N, ANTICIPATING THE 21ST CENTURY: COMPETITION POLICY IN THE NEW HIGH-TECH GLOBAL MARKETPLACE, *reprinted in* ANTITRUST & TRADE REG. REP. (BNA) No. 1765 (Special Supp.) (June 6, 1996) [hereinafter FTC Staff Report].

14. U.S. DEP'T OF JUSTICE, F.T.C., HORIZONTAL MERGER GUIDELINES (1997), *reprinted in* 4 Trade Reg. Rpt. (CCH) ¶ 13,104 [hereinafter MERGER GUIDELINES].

15. COLLABORATION GUIDELINES, 4 Trade Reg. Rep. (CCH) ¶ 13,160-161 [hereinafter COLLABORATION GUIDELINES].

have won since the early 1980s, the federal agencies might be accused of hastening the day (if it has not already arrived) that horizontal merger enforcement takes its place beside vertical and conglomerate merger enforcement as a relic of an bygone era. Moreover, its announced basis for considering efficiencies grew out of concerns that ignoring efficiencies in antitrust reviews might somehow put America at a disadvantage in the global marketplace. This fear seems highly unrealistic given the relative sophistication of American antitrust law and the even more restrictive approach taken by other antitrust authorities.[16] At the same time, there is a growing recognition that antitrust law needs to be more sensitive to efficiency benefits accruing from mergers particularly through innovation and product improvement.[17]

Anyone looking for a roadmap through the efficiencies thicket, however, will be disappointed by the agencies' revisions to the Merger Guidelines. While they tackle several of the thornier issues, few are decisively resolved. Though drafters assert that they add clarity and consistency to the merger investigations,[18] many critical questions are left unaddressed or are dealt with in contradictory or opaque language. The net effect is to open the door to a wide-ranging inquiry by courts or sister antitrust enforcement agencies that may not feel constrained by the policy choices or administrative convenience-driven distinctions that the FTC and Department of Justice decided to draw. The following section describes some of the controversy-laden aspects of the revisions:

*The Welfare Standard to Be Applied*. This application of the concept of efficiency is inextricably linked to one's view of which concept of welfare the Clayton Act was designed to protect.[19] Professor Lande and Fisher have persuasively argued that Congress' primary concern with regard to anticompetitive mergers focused on preventing transfers of wealth from

16. *See* Eleanor M. Fox, *Antitrust, Competitiveness and the World Arena: Efficiencies and Failing Firms in Perspective*, 64 ANTITRUST L.J. 725 (1996).

17. *See, e.g.*, Timothy Muris, *The Government and Merger Efficiencies: Still Hostile After All These Years*, 7 GEO. MASON L. REV. 729 (1999); Robert Pitofsky, *Proposals for Revised United States Merger Enforcement in a Global Economy,* 81 GEO. L.J. 195 (1992); Joseph Kattan, *Efficiencies and Merger Analysis,* 62 ANTITRUST L.J. 513 (1994). *See also* Joseph F. Brodley, *Proof of Efficiencies in Mergers and Joint Ventures*, 64 ANTITRUST L.J. 575 (1996). The seminal proposal for an explicit trade off between efficiency benefits and competitive harms is found in the scholarship of Oliver E. Williamson, *see, e.g.*, *Economies as an Antitrust Defense Revisited,* 125 U. PA. L. REV. 699 (1977).

18. Robert Pitofsky, *Efficiencies in Defense of Mergers: Two Years After,* 7 GEO. MASON L. REV. 485 (1999).

19. The Report notes the variety of academic views on the purposes and welfare objectives of the Clayton Act. FTC Staff Report, *supra* note 13, § I-B.

consumers to producers.[20] Others claim that the proper economic analysis centers upon allocative efficiency and hence consideration of gains accruing to producers as well as consumers is appropriate.[21] The revisions to the Merger Guidelines appear to adopt a consumer-focused welfare standard as the principal criterion for evaluating efficiencies, but do not entirely foreclose the possibility of applying a total surplus test that would countenance mergers that enhance market power and do not reduce consumer prices but lower total firm costs (and increase its profits). Hence the Guidelines state that the agencies will investigate whether proffered efficiencies "likely would be sufficient to reverse the merger's potential to harm consumers in the relevant market, e.g., by preventing price increases in that market."[22] Yet they go on to state that the agencies "also will consider the effects of cognizable efficiencies with no short-term direct effects on price in the relevant markets."[23] This may signal receptiveness, though on terms not yet specified, to considering efficiencies under a total surplus test and thus may permit consideration of fixed cost savings which are not normally considered under the short-term, price-effect test.[24]

*Timing*. While providing that an ameliorating price effect must be felt in the "short term," this proviso is qualified in a number of ways. For example, the Merger Guidelines state the standard would apply "in most cases," and that "delayed" efficiency benefits will be given less weight.[25] Moreover, the time period envisioned by the phrase "short term" is not defined. Whether the time horizon used in entry analysis section of the Guidelines (up to two years) is appropriate is unclear.[26]

20. Alan A. Fisher & Robert H. Lande, *Efficiency Considerations in Merger Enforcement*, 71 CAL. L. REV. 1580, 1592 (1983) (Congress' primary concern was with "market power that would unfairly transfer wealth from consumers to monopolists"). *See, e.g.*, STEPHEN ROSS, PRINCIPLES OF ANTITRUST LAW (1993) (legislative history suggests Congress would allow efficiency defense only for a merger of small firms); BORK, *supra* note 1, at 50-71 (arguing that narrowly defined consumer welfare, economy-wide allocative efficiency, is the only appropriate goal); Derek C. Bok, *Section 7 of the Clayton Act and the Merging of Law and Economics*, 74 HARV. L. REV. 226, 318 (1960) ("The possibility of lower costs was brushed aside in the legislative deliberations and there is every reason to believe that Congress preferred the noneconomic advantages of deconcentrated markets to limited reductions in the cost of operations.").

21. BORK, *supra* note 1, at 50-71 (arguing that narrowly defined consumer welfare, economy-wide allocative efficiency, is the only appropriate goal).

22. MERGER GUIDELINES, *supra* note 14, § 4.

23. *Id.* § 4 n.37.

24. Gregory J. Werden, *An Economic Perspective on the Analysis of Merger Efficiencies*, 11 ANTITRUST 12 (Summer 1997).

25. MERGER GUIDELINES, *supra* note 14, § 4.

26. *Id.* § 3.

*Which Efficiencies Count?* The Guidelines list several criteria for efficiencies that will be "cognizable." First, they must be "merger specific," that is, they must be likely to be accomplished through the merger and unlikely to be accomplished in the absence of the merger or through other means having less anticompetitive effects.[27] The Guidelines contemplate the possibility of achieving efficiencies by alternative means such as licensing or partial divestitures. At the same time, they disavow requiring alternatives that are not "practical" or "insist[ing] on a less restrictive alternative that is merely theoretical."[28]

A second criterion is that efficiencies be "verifiable." By this, the Guidelines intend that merging parties must substantiate their claims in a manner that permits the agencies to verify the likelihood, magnitude and cost of the efficiencies, the manner in which they will enhance incentives and abilities to compete, and the reasons why they are merger specific. While the Guidelines do not purport to frame questions in legal terms that a court might employ, it is notable that language requiring "clear and convincing evidence," contained in earlier government guidelines was dropped in an earlier iteration of the Guidelines.[29] At a minimum this change signaled a greater receptiveness to efficiencies despite continuing difficulties in proof.

Finally, the Guidelines list favored and disfavored efficiencies. Several prominent commentators have endorsed a categorization approach that classifies efficiencies based on their relative importance and susceptibility of proof and contemplates that antitrust tribunals should, as a matter of law, limit the defense according to these classifications. For example, Professor Areeda and his co-authors proposed that economies of scale and scope should generally be recognized, while economies in distribution, promotion and R & D which present relatively weak cases for consideration should be subject to more rigorous analysis. Others, such as managerial economies and savings in capital cost, procurement, or overhead, should generally not be recognized.[30] By contrast, the Guidelines stop short of ruling out categories of efficiencies, instead noting that certain kinds tend to be less likely to be cognizable, verifiable or substantial than others.

*Efficiencies Outside the Relevant Markets.* Rather surprisingly, the Guidelines indicate that the agencies will consider whether strong efficiencies found in markets other than those in which the merger may have anticompetitive effects outweigh the potential harms to competition. Several

27. *Id.* § 4.

28. *Id.*

29. 4 Trade Reg. Rep. (CCH) ¶ 13,103 [hereinafter 1984 GUIDELINES].

30. 4A PHILLIP AREEDA ET AL., ANTITRUST LAW ¶ 975 (1998); *see also* Brodley, *supra* note 17, at 579-82 (efficiencies defense should recognize production and innovation efficiencies, reject pecuniary and managerial economies, and admit capital raising economies only on a strong showing that they are real economies).

caveats apply, however. For example, the magnitude of the efficiencies must be large and the risk of anticompetitive harm small. Also, the markets must be "inextricably linked,"[31] and the government reserves its option of arguing that such effects should be given no weight in court,[32] at least when exercising prosecutorial discretion. However, the agencies may elect to trade off efficiencies in one market against another.

*How are efficiencies to be weighed?* The Guidelines seem to suggest that the agencies do not intend to measure or weigh efficiencies and anticompetitive harms in an attempt to calculate the "welfare trade-off."[33] In rather opaque terms, they sketch an analytic process that evaluates the effect of efficiencies on the overall competitiveness of the market after the merger.[34] At the same time, however, much of the language of the Guidelines is couched in terms of undertaking just such a quantitative comparison.[35] For example, the Guidelines are clear that efficiency claims must be commensurate with potential harms. In this regard, a sliding scale analysis is employed: large anticompetitve effects require "extraordinarily great" efficiencies. Moreover, efficiencies "almost never" justify mergers to monopoly. By their own account therefore, the Agencies envision some quantitative assessment, however crude, of losses and gains attributable to mergers.

### *Proof Burdens and Presumptions*

The Merger Guidelines are conspicuously silent on the important questions of what proof burdens and presumptive rules should apply to the efficiencies analysis. Indeed, the 1992 Merger Guidelines[36] removed the requirement of prior guidelines that efficiencies be proved by "clear and convincing evidence."[37] This seems to reflect more than the disinclination of the agencies to allocate burdens of proof in their guidelines. According to a former Assistant Attorney General, this change was made to allay concerns that the

31. MERGER GUIDELINES, *supra* note 14, § 4.

32. *Id.*

33. *See* Oliver E. Williamson, *Economies as An Antitrust Defense: The Welfare Trade-Offs*, 58 AM. ECON. REV. 18 (1968); *see also* Muris, *supra* note 17.

34. MERGER GUIDELINES, *supra* note 14, § 4 (The agencies "will not simply compare the magnitude of cognizable efficiencies with the magnitude of the likely harm absent the efficiencies. The greater the potential adverse competitive effect of the merger [as indicated by concentration data and analysis of effects and entry conditions] the greater must be cognizable efficiencies.").

35. *See* MERGER GUIDELINES, *supra* note 14, § 4 (showing of "extraordinarily great" efficiencies required to forestall challenge where anticompetitive effects are "particularly large" are "most likely to make a difference . . . when the likely adverse competitive effects, absent the efficiencies, are not great").

36. 4 Trade Reg. Rep. (CCH) ¶ 13,104.

37. 1984 GUIDELINES, *supra* note 29.

government was not sufficiently recognizing efficiencies and to make it clear that efficiencies would be accorded the same significance as other factors.[38]

*Paths Not Taken*

The revisions declined to follow recommendations that would have confined the inquiry to a set of limited questions that avoid explicitly balancing efficiencies against anticompetitive harms or would defer such reviews until after the merger had been consummated. For example, the FTC Staff Report proposed a two-part test that would require that proponents of proposed mergers to: (1) credibly demonstrate that the merger will create efficiencies; and (2) show how the resulting efficiencies will reduce the likelihood that any potential anticompetitive effects will arise from the merger and/or will improve the competitive dynamic in the postmerger market.[39] The merging parties would still bear the burdens of demonstrating the efficiencies and establishing that they cannot reasonably be achieved through less restrictive means. In addition, the FTC Staff Report seemed to suggest that proposed justifications should be subject to the test of whether proffered efficiencies are likely to change the merged firms' incentives and abilities so as to deter the possible exercise of market power.[40] This limited approach neatly avoids having to "balance" (and hence specifically calculate the magnitude of) efficiencies and anticompetitive losses or to evaluate whether cost savings will be "passed on" to consumers. Under this methodology, the clearest case for applying the defense occurs where it can be shown that efficiencies exert a positive effect on competition by deterring the exercise of market power. For example, mergers of non-leading firms may enhance competition by making them more formidable rivals, less likely to collude or passively accept price leadership by the dominant firm(s). Several other proposals have been advanced to develop structured, truncated evaluations of efficiencies that rely on classifications, presumptive rules and other methodologies but stop short of attempting to balance efficiencies against harms.[41]

Another road not taken by the agencies is the use of a subsequent review process to evaluate claims by merging parties. The FTC Staff Report recommended that in certain cases, parties should be allowed to consummate a proposed merger subject to an agreement. The FTC or DOJ would then review

38. FTC Staff Report, *supra* note 13, ch. 2, § III-H, n.156 (quoting James Rill, a former Assistant Attorney General of the Antitrust Division).

39. FTC Staff Report, *supra* note 13.

40. *Id.*

41. *See, e.g.*, Ann I. Jones, *Comments for the Federal Trade Commission*, FTC Hearings. (visited Mar. 20, 2000) <http://www.ftc.gov/opp/global/jones_ai.htm>. *See also* Statement of Robert Lande at FTC Hearings, (visited May 1, 2000) <http://www.ftc.gov/opp/global/GC111495.htm>; Robert Lande, Remarks at the meeting of the Federal Trade Commission on Global & Innovation-based Competition (Nov. 14, 1995) (transcript available at http://www.ftc.gov).

*ex post* whether the merger actually resulted in the claimed efficiencies. Under this procedure, the merged entity would be at risk if the claimed efficiencies failed to materialize or if anticompetitive effects arose from the merger. Advocates point out that this procedure reduces the incentives for merging firms to overestimate efficiency gains and counters the inherent uncertainty of predicting efficiencies *ex ante*. This approach was tested in the Hoechst/Marion Merrell Dow merger in which Hoechst was allowed to consummate the merger before the FTC had completed its investigation.[42] The FTC agreed to allow the merger to proceed subject to the acquirer's agreement to divest any of a predefined list of drugs which the FTC could later determine in its sole discretion were necessary to divest. In a similar vein, several state attorneys general have conditioned approval of mergers on monetary settlements predicated on promised efficiency savings.[43]

Despite a fair amount of enthusiasm for this idea in academic circles,[44] it was regarded by the FTC as impractical because of problems associated with monitoring the business affairs of the merged entity, difficulties inherent in unscrambling completed mergers, and the reluctance of judges to take on supervisory responsibilities of this sort. However, the Report suggested that the procedure might be most appropriate for joint ventures and mergers in which the parties volunteer and make a credible commitment to divest if anticipated efficiencies are not realized. In view of the criticism offered by a number of practitioners that the agencies do not follow their own guidelines and almost never conclude at the investigative stage that efficiencies will save an otherwise anticompetitive merger,[45] this approach would have the salutary effect of forcing both sides to perform the efficiencies inquiry in an appropriate manner.

### *B. Efficiencies in Joint Venture Analysis*

When looking at the agencies' treatment of efficiencies in joint venture analysis, one finds an unambiguous endorsement of balancing. For example, in the Statements of Antitrust Enforcement Policy in Health Care, the agencies repeatedly state that an assessment of a health care joint venture requires a balancing of the joint venture's likely pro-competitive efficiencies against any

42. Hoechst AG, C-3629, 5 Trade Reg. Rept. (CCH) (FTC Dec. 5, 1995).

43. *See, e.g.*, Pennsylvania v. Capital Health Sys. Servs., 1995-2 Trade Cas. (CCH) ¶ 71,205 (M.D. Pa. 1995). *See generally* Thomas L. Greaney, *Regulating for Efficiency Through the Antitrust Laws*, 1995 UTAH L. REV. 465, 486-89 (1995).

44. *See* Brodley, *supra* note 17; Pitofsky, *supra* note 17. *But see* Eleanor M. Fox, *Antitrust, Competitiveness and the World Arena: Efficiencies and Failing Firms in Perspective*, 64 ANTITRUST L.J. 725 (1996).

45. *Mergers and Acquisitions: Trends in Antitrust Oversight of Mergers, Joint Ventures Discussed by Practitioners,* Antitrust Trade Reg. Rep. (BNA) (Mar. 25, 1999).

likely anticompetitive effects. For example, in assessing the impact of provider controlled networks, the Policy Statements provide as follows:

> *Step 3: Evaluate the Impact of Procompetitive Efficiencies.* This step requires an examination of the joint venture's likely procompetitive efficiencies, and the balancing of these efficiencies against any likely anticompetitive effects. The greater the venture's likely anticompetitive effects, the greater must be the venture's likely efficiencies.[46]

Essentially identical analytical processes are recommended for evaluating health care high technology joint ventures.[47] The Department of Justice Intellectual Property Guidelines likewise state that the agencies will balance procompetitive efficiencies and anticompetitive effects to determine the probable net effect of restraints in licensing arrangements on competition, but add the caveat that this comparison "is necessarily a qualitative" one, a provision not found elsewhere in Department guidelines.[48]

In their most recent guidelines, the Antitrust Guidelines for Collaboration Among Competitors,[49] the agencies provide the most detailed statement of their views on weighing efficiencies generated by joint ventures. Following generally the Merger Guidelines' approach, the Collaboration Guidelines require proof of "cognizable efficiencies" that are verifiable and reasonably necessary, and then go on to state:

> [T]he Agencies assess the likelihood and magnitude of cognizable efficiencies and anticompetitive harms to determine the agreement's overall actual or likely effect on competition in the relevant market. To make the requisite determination, the Agencies consider whether cognizable efficiencies likely would be sufficient to offset the potential of the agreement to harm consumers in the relevant market, for example, by preventing price increases (footnote omitted).
>
> The agencies' comparison of cognizable efficiencies and anticompetitive harms is necessarily an approximate judgment. In assessing the overall competitive effect of an agreement, the Agencies consider the magnitude and likelihood of both the anticompetitive harms and cognizable efficiencies from the relevant agreement.

46. DEPARTMENT OF JUSTICE AND FEDERAL TRADE COMM'N, STATEMENTS OF ANTITRUST ENFORCEMENT POLICY IN HEALTH CARE (1996), 4 Trade Reg. (CCH) ¶ 13,153 [hereinafter Health Policy Stmt.].

47. Health Policy Stmt. 2, Statement on Hospital Joint Ventures Involving High Technology or Other Expensive Equipment; Health Policy Stmt. 3, Statement on Joint Ventures Involving Specialized Clinical or Other Expensive Services.

48. DEP'T OF JUSTICE, ANTITRUST GUIDELINES FOR THE LICENSING OF INTELLECTUAL PROPERTY (1995).

49. Draft of ANTITRUST GUIDELINES FOR COLLABORATION AMONG COMPETITORS, issued Oct. 1, 1999.

It thus appears that the agencies have pulled back from earlier policy statements that endorsed an open-ended approach to balancing. In keeping with the analysis contained in the Merger Guidelines, joint ventures efficiencies apparently will be held to standards of cognizability and reasonable necessity. The Collaboration Guidelines also include an appropriate caveat that the process entails approximate judgments, and seemingly signal that they may not always essay even rough quantitative assessments. At the same time, however, the truncated analyses contained in Collaboration Guidelines evidence no reliance on presumptive approaches or other devices that might usefully cabin the factfinders inquiry. It is not entirely clear whether this approach reflects refinements in the agencies' methodology for analyzing efficiencies or whether it is dictated by the special circumstances created by joint ventures. Although a more lenient approach for joint ventures might be justified because of their less permanent nature and hence lower risk of harm, realizing efficiencies nonetheless may be problematic in the joint venture setting because of the parties' unwillingness to fully share advantages and learning in such an enterprise.[50]

### *C. Assessing the American Approach*

Despite extensive attention paid to the subject, proponents of an expanded efficiencies defense for mergers and joint ventures have failed to muster a convincing showing that prior antitrust policy chilled parties from undertaking mergers that would benefit consumers or that government action blocked such mergers.[51] Given the generous levels of concentrations permissible under current merger law (which most commentators agree allows parties to capture most scale and scope economies),[52] and the leniency with which contemporary antitrust doctrine interprets mergers,[53] it is not likely that many mergers fail to achieve efficient size. Further, the evidence points strongly to the conclusion that determining *ex ante* whether a merger will generate significant efficiencies is an extraordinarily difficulty task. Thus, studies demonstrating that a large number of mergers fail to realize projected efficiency gains illustrate that those in the best position to assess the probability and magnitude of prospective efficiencies, the merging parties themselves, routinely err.[54] Indeed, by some

50. *See generally* Brodley, *supra* note 17.

51. For broad assurances that efficiency trade offs can be performed, see Robert Pitofsky, *FTC Staff Report on Competition Policy: Six Months After*, Remarks Before the ABA Section on Antitrust Law (Nov. 7, 1996). For strong expressions of skepticism, see Brodley, *supra* note 17; AREEDA ET AL., *supra* note 30.

52. AREEDA ET AL., *supra* note 30.

53. Eleanor M. Fox, *Antitrust, Competitiveness and the World Arena: Efficiencies and Failing Firms in Perspective*, 64 ANTITRUST L.J. 725 (1996).

54. DAVID J. RAVENSCRAFT & F.M. SCHERER, MERGERS, SELL-OFFS, AND ECONOMIC EFFICIENCY (1987); *After the Deal,* ECONOMIST, Jan. 9, 1999 (explaining that "study after study

estimates, sixty to eighty percent of all mergers prove unsuccessful.[55] When one expands the inquiry into critically important, but necessarily inchoate, dimensions of efficiency such as quality of health care products and services or synergies resulting from shared know-how, technology or research, the level of imprecision and subjectivity in efficiency analysis escalates geometrically.[56] Adding the further "dynamic" dimension of assessing the degree to which efficiencies may or may not diffuse throughout markets as a result of a merger or joint venture also seems essential,[57] though the process invites complexities likely to exceed he capacities of the courts. With the empirical record raising legitimate questions about how effectively courts and enforcement agencies can predict and quantify efficiencies, it would seem appropriate to hold proponents of a more complete trade-off analysis to prove the predictive reliability of their methods.

On the other side of the balancing ledger, the prospects for accurate analysis appear even bleaker. Neither the measures of concentration nor other structural indices give a very accurate picture of the magnitude of competitive harm resulting from mergers. Imprecision in the definition of markets and calculation of concentration data, along with the lack of information about firm strategies, makes reliable estimates of the likely losses impossible.[58] Most courts seem to recognize this and thus resort to evidentiary or presumptive short cuts to avoid the process.[59] Even those that use the terminology of balancing are not actually assigning a common unit of measurement to the harms and benefits and then determining which outweighs the other.[60]

Another notable feature of the efficiency approach is the absence of useful rules for performing the inquiry. While the least-restrictive alternative test

of past merger waves has shown that two of every three deals have not worked . . . [although] buyers have justified deals by citing questionable synergies"). *See also The Case Against Mergers*, BUS. WEEK, Oct. 30, 1995 (noting that businesses often cannot predict accurately which mergers are likely to create efficiencies).

55. Brodley, *supra* note 17, at 576.

56. *See* Thomas L. Greaney, *Regulating for Efficiency in Health Care through the Antitrust Laws*, 1995 UTAH L. REV. 465, 491-92 (discussing the problems of performing efficiency analyses in the health care sector). *See generally* Joseph F. Brodley, *Proof of Efficiencies in Mergers and Joint Ventures*, 64 ANTITRUST L.J. 575 (1996).

57. Gary L. Roberts & Steven C. Salop, *Efficiency Benefits in Dynamic Merger Analysis*, WORLD COMPETITION (1996).

58. AREEDA ET AL., *supra* note 30, ¶ 976 (noting that "in the great majority of cases we can do no better than play a hunch about the magnitude of competitive harms resulting from a merger.").

59. *See* discussion of efficiencies defense in merger litigation *infra*; *see also* Brodley, *supra* note 17, at n.38 (survey of cases through 1996 involving efficiency defense, finding sixteen cases in which courts evaluated less restrictive alternatives and none which evaluated efficiencies in any meaningful way; one case, U.S. v. United Tote, Inc., 768 F. Supp. 1064 (D. Del. 1991), employing conclusory assessment of competitive effects and efficiency benefits).

60. AREEDA ET AL., *supra* note 30, ¶ 976.

avoids balancing, it cannot be said to constitute a substitute; at best it circumvents the inquiry, but provides no assurance that consumer interests will be addressed in merger reviews.[61] Merger simulations using econometric methodologies does not afford a silver bullet for evaluating efficiencies in mergers and joint ventures. Those methodologies provide only insights into the anticompetitive effects of the merger and are unhelpful regarding the quantification of efficiencies and are subject to considerable discretion in application.[62] The conclusion that balancing "is simply not what courts are capable of doing"[63] seems inescapable.

How are courts likely to react to the Agencies' approach to efficiencies? Although the several merger and joint venture guidelines expressly disavow any intention to describe how the agencies will present evidence in litigating merger cases,[64] courts frequently cite the Guidelines and sometimes hold the government to those standards where it appears they are advocating a different position in court.[65] It is far from clear that, in performing efficiency analyses, courts will feel constrained to follow the Guidelines' limitations which are not sharply defined or clearly explained or are based on considerations of administrative convenience. In sum, although they commonly use shortcuts to truncate (or sidestep) the inquiry, courts generally perceive their task as conducting an open-ended balancing of harms against savings and rarely resort to tools such as classifying efficiencies, use of the consumer standard or otherwise narrow the scope of the efficiency trade-off.

### *D. Efficiencies Analyses in Litigation*

Although the Supreme Court stated over forty years ago that "possible economies cannot be used as a defense to illegality in Section 7 merger cases," virtually all courts considering the issue in recent years have permitted an efficiencies defense at least to the extent that it may be used to rebut the government's prima facie case.[66] Courts tackling the efficiencies issue have

61. *Cf.* Brodley, *supra* note 56 at 585 (stating that the least restrictive alternative test "must lead either to strained applications or illfounded attempts to engage in explicit balancing").

62. *See* Craig W. Conrath & Nicholas A. Widnell, *Efficiency Claims in Merger Analysis: Hostility or Humility?*, 7 GEO. MASON L. REV. 685 (1995).

63. *Id.*; *see also* POSNER, *supra* note 2; BORK, *supra* note 1; Brodley, *supra* note 56 (noting that leading proponents fail to explicate how balancing might take place).

64. MERGER GUIDELINES § 0.1. Although efficiencies have influenced the FTC's decision not to challenge a few mergers since the amendments to the Merger Guidelines, the litigated cased decided since 1997 have not entailed the kind of balancing approach suggested by the guidelines. *See* Robert Pitofsky, *Efficiencies in Defense of Mergers: Two Years After*, 7 GEO. MASON. L. REV. 485 (1999).

65. *See, e.g.*, United States v. Waste Management, Inc. 743 F.2d 976, (2d Cir. 1984).

66. FTC v. Univ. Health, Inc., 938 F.2d 1206, 1222 (11th Cir. 1991) (defendant may rebut the government's prima facie case with evidence showing that the merger would create significant efficiencies in the relevant market); FTC v. Cardinal Health, Inc., 12 F. Supp.2d 45

several times found substantial efficiencies,[67] though sometimes mitigating that finding by concluding that the efficiencies were not merger specific or were equally likely to be forthcoming from competition in the market.[68] Others have rejected defendants' proffered efficiencies as speculative, unverified, or uncertain.[69] Commentators have noted the symmetry between the conclusions reached by courts on the competitive effects of mergers and their resolution of the efficiencies defense. Most courts finding substantial efficiencies do so only where they also conclude that the merger would not be likely to substantially lessen competition.[70]

For better or worse, hospital mergers have become a proving ground in American courts for weighing efficiencies in antitrust cases. These cases are instructive in that they demonstrate the unwillingness of antitrust tribunals to face up to the task of balancing efficiencies and the intractable nature of many of the factual issues that arise. As a result, most courts have employed evidentiary presumptions and relied on the placement of the burden of proof to evade trade off analyses.

In some respects, the hospital industry is well-suited for efficiencies analysis; in others, decidedly not. Clearly, the industry suffers from significant overcapacity attributable to government policies, inefficient reimbursement methodologies and rapid technological change causing shifts in where many procedures are performed.[71] Moreover, conditions on both the demand and supply side are changing rapidly to deal with the new environment. These cataclysmic changes occurring in heath care financing and delivery make it extraordinarily difficult to predict with confidence what kinds of savings are

(D.D.C. 1998) (recognizing defense but finding that substantial efficiencies that would be achieved by merger could also be attained by competitive process); FTC v. Staples, Inc., 970 F. Supp. 1066, 1090 (D.D.C. 1997) (considering but ultimately rejecting as unverified and not merger-specific defendants' claimed efficiencies); United States v. Long Island Jewish Hosp., 983 F. Supp. 121 (E.D.N.Y. 1997); *Cf.* FTC v. Coca-Cola Co., 641 F. Supp. 1128, 1141 (D.D.C. 1986) *vacated as moot*, 829 F.2d 191 (D.C. Cir. 1987).

67. *Cardinal Health, Inc.*, 12 F. Supp.2d 45; *Long Island Jewish Hosp.*, 983 F. Supp. 121. *See also* Tenet Healthcare Corp. v. FTC, 186 F.3d 1045 (8th Cir. 1999) (stating in dicta that district court should have paid greater attention to efficiencies).

68. *Cardinal Health, Inc.*, 12 F. Supp.2d 45.

69. FTC v. Tenet Healthcare Corp. 17 F. Supp.2d 937 (E.D. Mo. 1998), *rev'd on other grounds*, 186 F.3d 1045 (8th Cir. 1999); *Staples*, 970 F. Supp. at 1090.

70. Joseph Kattan, *Efficiencies and Merger Analysis*, 62 ANTITRUST L.J. 513, 516 (1994).

71. *See* Joe Sims, *A New Approach to the Analysis of Hospital Mergers,* 64 ANTITRUST L. J. 633 (1996) (contending that the peculiarities of hospital markets require altering application of conventional presumptions in merger analysis; also urging more receptive treatment of defendants' efficiency claims).

attributable to a given merger and what less restrictive alternatives might exist.[72]

Federal courts have closely examined defendants' efficiencies claims in seven hospital merger cases. In three of those cases, the district court made rather cursory findings to the effect that defendants had presented plausible efficiency claims.[73] One other district court relied in part on evidence of efficiencies in finding that the hospitals had rebutted the government's prima facie case,[74] and another endorsed in dicta the defendants' claim.[75] In the only appellate case,[76] three district court cases,[77] and several FTC administrative proceedings[78] on the subject, defendants' proof on the efficiencies has been found wanting. For their part, the federal enforcement agencies have taken the position that they may weigh efficiencies in deciding whether or not to challenge a merger,[79] while occasionally arguing that efficiencies considerations are not cognizable by federal courts.

Several observations may be made about the decided cases. First, with one exception, courts have followed a pattern of symmetry between their findings on the merits of the government's merger case and their treatment of efficiencies. That is, courts ruling for defendants on other grounds uphold their efficiency claims, while those concluding that the merger will lessen competition reject efficiencies claims.[80] Courts thus may be taking the easy way out on this complex issue.

Second, a number of courts have held defendants to a high standard of proof, e.g., "clear and convincing evidence" on efficiencies defenses.[81] The cases also sometimes fault defendants for failing to prove "net efficiencies":

72. *See* Thomas L. Greaney, *Night Landings on an Aircraft Carrier: Hospital Mergers and Antitrust Law*, 23 AM. J.L. & MED. 1991 (1997).

73. *See* FTC v. Freeman Hosp., 911 F. Supp. 1213 (W.D. Mo. 1995), *aff'd*, 69 F.3d 260 (8th Cir. 1995); United States v. Carilion Health Sys., 707 F. Supp. 840 (W.D. Va.), *aff'd*, 892 F.2d 1042 (4th Cir. 1989); FTC v. Univ. Health, Inc., 1991-1 Trade Cas. (CCH) ¶ 69,444 (S.D. Ga. 1991), *rev'd*, 938 F.2d 1206 (11th Cir. 1991).

74. FTC v. Butterworth Health Corp., 946 F. Supp. 2385 (W.D. Mich. 1996).

75. *See Long Island Jewish Hosp.*, 983 F. Supp. 121.

76. *See Univ. Health*, 938 F.2d 1206.

77. *Tenet*, 17 F. Supp.2d 937, United States v. Mercy Hosp., 902 F. Supp. 968 (N.D. Iowa 1995); United States v. Rockford Mem'l Corp., 717 F. Supp. 1251 (N.D. Ill. 1989).

78. American Medical Int'l, 104 F.T.C. 1, 219-20 (1984); Hospital Corp. of Amer. 106 F.T.C. 361 (1985). *See generally* Mary Lou Steptoe, Acting Director, Bureau of Competition, Federal Trade Commission, *Efficiency Justifications for Hospital Mergers*, Remarks before Practicing Law Institute (June 17, 1994).

79. Department of Justice and Federal Trade Commission, HORIZONTAL MERGER GUIDELINES § 4 (1992). The government's changing position on efficiencies is described in the FTC Staff Report, *supra* note 13, ch. 2, § I-C.

80. The lone exception is *United States v. Mercy Hospital*, 902 F. Supp. 968 (N.D. Iowa 1995).

81. *See, e.g.*, *Rockford Mem'l*, 717 F. Supp. at 1289; *Hospital Corp.* 106 F.T.C., at 361.

that is, in quantifying efficiencies, defendants neglected to deduct the cost of achieving savings from the total savings anticipated.[82] The latter has been an important issue as hospitals claiming efficiencies arising out of renovation and replacement of facilities must offset the costs of those improvements along with any changes in quality.[83] Other courts have relied upon credibility findings regarding the parties' experts or the probative value of the information on which they relied. Finally, many courts have noted that defendants have failed to prove that efficiencies would be passed on to the consumer. These techniques have enabled courts to evade the difficult factual inquiry into the magnitude of efficiencies and the degree of potential anticompetitive harm flowing from the merger.

Third, while a wide variety of efficiencies have been considered in various cases, those involving economies in scale and scope, as well as savings resulting from combined administrative functions, have proven the most successful.[84] Indeed, in litigation, the government has often conceded the validity of such efficiencies in principle while vigorously disputing their magnitude or the feasibility of their being implemented. As a general matter, the agencies take the position that preferred efficiencies include better use of fixed cost assets and elimination of duplicative services, while other kinds of efficiencies, such as savings in the cost of capital and shared inputs, are suspect, primarily because they can often be accomplished without merger. Scale economies and other savings, from consolidating programs operated at less than efficient levels, are readily identifiable and estimated.[85] Courts have been skeptical of purported savings resulting from improved information and use of "best practices" resulting from mergers, contending that such savings readily obtained through other means and were difficult to quantify.[86] Notably, in the most recent hospital merger case, the Eighth Circuit found that the lower court should have explicitly weighed quality-enhancing aspects of the merger against anticompetitive harms under an efficiency analysis.[87] Thus, the

82. *Id.*

83. For a good analysis of this issue, see Steptoe, *supra* note 78.

84. *See, e.g.*, *Univ. Health*, 938 F.2d 1206 (savings from eliminating equipment duplications and administrative savings); *Rockford Mem'l*, 717 F. Supp. at 1288 (elimination of duplicative services, consolidation of overhead); *Freeman Hosp.*, 911 F. Supp. 1213.

85. A clear explanation of the economist's methodology for appraising efficiencies in hospital merger cases is found in Barry C. Harris & William P. Hall, *Balancing Efficiencies and Competition in Hospital Mergers,* 8 A.B.A. SEC. ANTITRUST HEALTH CARE CHRON., No. 3, 2 (1994).

86. *Mercy Hosp.,* 902 F. Supp. at 987-89.

87. In *Tenet v. FTC*, the court stated as follows:

> We further find that although Tenet's efficiencies defense may have been properly rejected by the district court, the district court should nonetheless have considered evidence of enhanced efficiency in the context of the competitive effects of the merger. The evidence shows that a hospital that is larger and more efficient than Lucy Lee or

litigated cases have sidestepped many important but hard-to-quantify efficiencies.

Finally, in the hospital cases, the efficiencies defense has become an invitation to explicit regulation by court decree. In *F.T.C. v. Butterworth Health Corporation*,[88] for example, the court found that the merger would produce significant "capital avoidance" savings. Notably, the district court accepted the efficiencies defense without explicitly weighing the purported savings (found to be in excess of $100 million) against any specific finding of potential harm to competition. The potential harm to competition, the court acknowledged, was manifest in that case because the merger created a near monopoly in the relevant market. It found this risk mitigated by the merged hospital's not-for-profit status and the parties' voluntary commitment to take various steps to assure that prices would be kept low. Remarkably, these commitments, contained in a court-approved consent decree, include provisions freezing prices at pre-merger levels, limiting profit levels, assuring services to the medically needy, and establishing governance of the merged entity. In implicitly finding that efficiency savings would outweigh whatever competitive harms might result from the merger, however, the court explicitly acknowledged its inability to calculate net efficiencies or to perform the welfare trade-off.[89] Instead, it noted a disparity in the quality of the studies performed by the parties' experts, voiced its greater confidence in the defendants' expert, and gave considerable weight to its own impressions based on a tour of the hospital facilities in the relevant market. Other district courts have likewise used rather vague findings of efficiencies to buttress their conclusions that the merger would not lessen competition.[90]

The rather loose and imprecise approach to "weighing" efficiencies against harms seen in the hospital merger cases, though perhaps understandable in view of the uncertainties involved, is a far cry from the balancing anticipated by proponents of the efficiencies defense. In addition, it should be emphasized that assessing efficiencies is particularly hard in a case in which the market is changing rapidly. For example, the court opined that Butterworth would likely

> Doctors' Regional will provide better medical care than either of those hospitals could separately. The merged entity will be able to attract more highly qualified physicians and specialists and to offer integrated delivery and some tertiary care.

186 F.3d 1045, 1054 (8th Cir. 1999).

88. 946 F. Supp. 1285 (W.D. Mich. 1996).

89. The court stated:

> Because measuring the efficiencies of a proposed transaction is inherently difficult and because both sides' estimates are clearly based in some measure on speculative self-serving assertions . . . the [c]ourt finds it neither appropriate nor necessary to engage in a detailed evaluation of the competing views.

*Butterworth*, 946 F. Supp. at 1301.

90. *See supra* note 73.

proceed with plans to renovate and expand its facilities in order to compete with the new state of the art facility planned by Blodgett, concluding "a medical arms race would thus continue, at great expense to defendants and ultimately to consumers."[91] Such findings obviously rest on a myriad of assumptions about the pace of development of managed contracting, the current competitiveness of the market, and other factors. Confident judgments about how much would be spent in the future absent the market seem so speculative as to call into question the capacity of courts to make such predictions confidently in a changing market.

## II. TREATMENT OF EFFICIENCIES UNDER THE EU MERGER REGULATION

Contrary to assertions by American antitrust officials that competition authorities in the Commission of the European Union and its member states regularly take efficiencies into account when reviewing mergers,[92] efficiencies have played a negligible role in European analyses. Though this claim was made to justify an expanded role for efficiencies in American enforcement, it does not withstand close scrutiny. This section argues that EU competition policy has refrained from adopting an explicit efficiencies defense and that efficiencies have rarely, if ever, played an important role in decisions to clear mergers or accept restructuring proposals.

Mergers with a "community dimension"[93] in the EU are governed by the Merger Regulation adopted by the Council of Ministers in 1989.[94] The regulation mandates prior notification of proposed "concentrations" to the competition directorate (DG-IV) of the Commission. A substantive review of mergers is generally performed by the Merger Task Force at the Commission. The Merger Regulation governs "concentrations" and mandates an inquiry as to whether they are compatible with the common market, interpreted to prohibit any that "creates or strengthens a dominant position as a result of which effective competition would be significantly impeded in the common market or in a substantial part of it."[95] Although the Merger Regulation does not speak to the issue of extraterritorial enforcement, the Commission has invoked jurisdiction in a number of recent cases.[96]

91. *Butterworth*, 946 F. Supp. at 1301.

92. Remarks of Robert Pitofsky, Chairman, Federal Trade Commission, *The Effect of Global Trade on United States Competition Law and Enforcement Policies* (Oct. 15, 1999).

93. Council Regulation 1310/97 of June 30, 1997 O.J. (L 180) (amending Merger Regulation to reach mergers in which the undertakings have a combined worldwide turnover of at least $2.5 billion ECU; in which each undertaking has an EU wide turn over of at least 100 million ECU; and other requirements respecting turnover in at least three Member States).

94. Commission of Council Regulation 4064/89.

95. *Id.*

96. Jurisdiction has been asserted in cases in which the merging parties have limited assets in the EU, Boeing/McDonnell Douglas; and in which the assets of the merging parties giving rise

The Merger Regulation contains no provision governing efficiencies. However, under Article 2(1)(b), the Commission is directed to consider whether a concentration will likely result in "the development of technical and economic progress provided that it is to consumers' advantage and does not form an obstacle to competition."[97] The language of Article 2(1)(b) is derived from Article 85(3) and is construed in light of the decisions of the European Court of Justice and other jurisprudence surrounding that doctrine.[98] Although Article 85(3) has had some influence on the development and analysis of agreements in the EU, the concept of technical and economic progress has played almost no role in substantive merger analysis by the Commission. Indeed the history[99] and text[100] of Article 2(1)(b) does not support explicit trade-offs between efficiencies and market power. Consequently, most leading commentators agree that no efficiency defense can be found in EU merger analyses to date.[101]

A review of the handful of cases in which the Commission has considered potential advantages associated with technical and economic progress resulting from mergers, reveals that the factor has not played a role in any clearance by the Merger Task Force and at most appears to have been considered as a factor

to competition concerns are located outside of the EU, Gencor/Lonrho, Case IV/M619 (Apr. 24, 1996) 1997 O.J. (L11) 30.

97. EU Merger Regulation Article 2(1)(b).

98. *See* Commission of European Communities, Nineteenth Report on Competition Policy 266 (1990).

99. Earlier drafts of the Merger Regulation contained broad language that might have allowed an efficiencies trade off, as well as non-economic factors, to trump a finding of market dominance. Deletion of this language, along with amendments rendering the final text of the Article 2(1)(b) moot on the use of technical and economic factors once dominance is found, make it clear that the regulation does not support a trade off analysis. *See* Pierre-Emmanuel Noel, *Efficiency Considerations in the Assessment of Horizontal Mergers under European and U.S. Antitrust Law*, 8 E.C.L. REV. 498, 503-04 (1997); CHRISTOPHER JONES & F. ENRIQUE GONZALEZ-DIAZ, THE EEC MERGER REGULATION 153-58 (1992); *see also* SIR LEON BRITTAN, COMPETITION POLICY AND MERGER CONTROL IN THE SINGLE EUROPEAN MARKET 47 (1991). ("[N]o words plucked from the [Merger] Regulation can give rise to a defence against the finding that there is a dominant position.").

100. Economic and technical benefits are only relevant to the extent that they do not "form an obstacle to competition." EU Merger Regulation, Article 2(1)(b).

101. *See, e.g.*, JONES & GONZALEZ-DIAZ, *supra* note 99, at 156 ("there can be no efficiency defence as such to a finding of durable dominance under the regulation"); C.J. COOK & C.S. KERSE, E.C. MERGER CONTROL 167 (1996) ("There is no efficiency defence in the Regulation, in the sense recognised in North American merger controls, and none has emerged from the Commission's application of it so far."); Noel, *supra* note 99, at 512 (finding "no 'efficiency defence' as such" in EU merger regulation). *See also* BARRY E. HAWK & HENRY L. HUSER, EUROPEAN COMMUNITY MERGER CONTROL: A PRACTITIONER'S GUIDE 265 (1996) (technical and economic progress and efficiencies have played only "minor role" in Commission enforcement); Camesasca, *supra* note 12 (finding an "implicit efficiencies defence" sometimes used to "tip the balance" against a finding of dominance).

militating in favor of acceptance of remedial undertakings to allow mergers to proceed. In the leading case, *Aerospatiale-Alenia/deHavilland*,[102] the Commission examined a variety of efficiency-related advantages of the proposed consolidation including improved management, cost savings in parts procurement and marketing, and protection against currency fluctuations. However, the Commission rejected the importance of such advantages because of the merger's propensity to enhance the dominant position of the combined firm will be necessary. The decision refrained from endorsing the principle of employing efficiencies as a counterweight to competitive concerns,[103] and its holding seemed to imply that most efficiency arguments will be unavailing in the case of a finding of dominance.[104] Likewise, in *MSG Media Service*[105] the Commission concluded that a joint venture would improve the prospect for the spread of digital pay television through improved administrative and technical support, but stated that such a factor should be considered only where the concentration did not create or strengthen a dominant position or hinder effective competition. In a number of other cases, the Commission also expressly noted the potential for improvements in firm efficiency that would enhance technological and economic progress but resisted clearance on those grounds.[106] Other Commission decisions can be seen to take efficiencies improvements into account "between the lines" by incorporating analyses of the dynamics of markets in entry analyses, market definition and evaluation of the significance of market share data.[107] Finally, in a number of cases the Commission has employed findings of enhancement of efficiencies to bolster its conclusion that the merger will increase or create market dominance.[108]

The EU's reluctance to adopt an explicit efficiencies defense or to incorporate efficiencies into its assessment of competitive effects may be as much attributable to the fact that the Commission has until recently largely

102. Case No. IV/M.053 (Oct. 2, 1991), OJ L334/42 (Dec. 5, 1991).

103. *See id.* ¶ 65 ("Without prejudice as to whether [efficiency] considerations are relevant for assessment under Article 2 of the Merger Regulations, such cost savings would have a negligible impact on the overall operations" of the merged entity).

104. *See* JONES & GONZALEZ-DIAZ, *supra* note 99, at 158 (explaining that the *de Havilland* decision confirms that "there can be no efficiency defence where there is clear market dominance").

105. Case No. IV/M.469 (Nov. 9, 1994), O.J. L364/1 (Dec. 31, 1994).

106. *See* Accor/Wagon Lits, Case No. IV/M.126 (Apr. 28, 1992), O.J. L 204/1 (July 21, 1992) (insufficient proof that claimed efficiencies would outweigh anticompetitive effects); Nordic Satellite Distrib., Case No. IV/M.490 (1995) (vertical integration creating significant scale and scope efficiencies insufficient given propensity to strengthen dominant position).

107. *See* Camesasca, *supra* note 12, at 25-27 (summarizing cases in which efficiencies issues played an important role in Commssion's dynamic analysis of markets and competitive effects).

108. *See, e.g.*, Du Pont/ICI, Case No. IV/M, 214 (Sept. 30,1992), O.J. L 7/13. *See* Frederick Jenny, *EEC Merger Control: Economies as an Antitrust Defense or an Antitrust Attack?* 1992 FORDHAM CORP. L. INST. 591 (1993).

focused on cases involving single firm, rather than collective, dominance. Mergers enhancing risks of oligopolistic market power may raise somewhat different efficiencies issues in that efficiencies gains arising from a merger that are not readily duplicated by rivals may reduce the likelihood and ease of coordination.[109] Hence, a stronger case for considering efficiencies may present itself as the Commission evaluates more collective dominance cases. It is important to note, however, that such evaluations going to the likelihood of the exercise of market power can be made independently and without need to undertake a trade-off analysis. Hence, the EU's increasing focus on collective dominance does not support adoption of the overall analytic approach taken by the American antitrust authorities.

In sum, owing to its different history and goals, merger policy in the EU has followed a trajectory that has to date steered away from the quagmire of an explicit efficiencies defense. Undoubtedly, efficiencies have played a part in many aspects of the Commission's application of the merger laws, but they have never risen to the level of offsetting competitive harms associated with a merger. Hence, far from justifying the American movement toward fuller evaluation of efficiencies through explicit trade off analysis, the roles of the two authorities appear to be just the opposite. The EU may now be in a position of facing pressures to follow suit to keep up with its American counterpart and perhaps to leave itself the "flexibility" to endorse mergers that suit political rather than competition-focused goals.

## III. RISKS OF EU ADOPTION OF THE AMERICAN STANDARD

Embracing the American efficiencies defense to mergers and joint ventures would serve neither the EU's interest in effective antitrust enforcement nor promote the need for a more certain set of rules governing border-spanning mergers. First, as discussed in Section I of this essay, a myriad of normative judgments and policy choices confront antitrust authorities devising an explicit efficiencies defense. The vigorous disagreement among academics and policy makers concerning the appropriate welfare standard to be applied should give pause to EU competition authorities. Extensive debate on that subject has not produced consensus, as first principles and normative judgments play an important role in choosing a standard. The significance of the choice of welfare standard cannot be overstated, as it strongly influences the complexity of the efficiencies inquiry and the ease with which the defense can be asserted. Leaving the standard ambiguous, as the United States has apparently done, may invoke ad hoc applications of the doctrine and raise the cloud of "political" jurisprudence.

109. *See* HAWK & HUSER, *supra* note 101, at 267-68.

Second, the *ex ante* predictions required for analyzing efficiencies are notoriously imprecise. The absence of a proven track record of forecasting efficiencies and the dearth of accepted methodologies for doing so counsel caution before enshrining a broad policy that will absolve otherwise anticompetitive mergers. Where empirical judgments necessary to bring enforcement actions are prone to high rates of error, merging parties will face strong incentives to opportunistically seek out mergers that they would otherwise forego. In this connection, it is notable that at many junctures the American efficiency defense leaves wide discretion to the decisionmaker. The approach of the Merger Guidelines has been to weigh heavily administrative concerns and adopt pragmatic solutions, while leaving open the opportunity to consider broad evidence where deemed appropriate. While flexibility is desirable at the prosecutorial stage, the absence of reviewable standards and clearly articulated doctrine poses obvious problems when the matter appears before antitrust tribunals. In this regard, the experience of the American courts is instructive and discouraging. Faced with the inherent uncertainties and complexities of the efficiency inquiry, courts have resorted to evidentiary shortcuts and other measures that fall far short of a meaningful balancing of efficiencies and harms. In some instances, they have developed tests that make little economic sense (e.g., the requirement that efficiencies be passed on to consumers). In others they have resorted to evidentiary sleight of hand (e.g., relying on findings concerning the credibility of experts or assigning dispositive weight to internal studies). In the end, the results of judicial efficiencies inquiries seem pre-ordained by the courts' conclusions on competitive effects.

The impact of a potent efficiencies defense on reviews of transnational mergers and joint ventures raises a host of additional concerns. The mix of inherently uncertain factual determinations and discretion-laden decisional rules would seem an open invitation to ad hoc judgments. Given the inevitable political and nationalist undercurrents when governments review transnational combinations, the efficiencies defense would seem to afford an all-too-convenient tool for disguising industrial policy as competition analysis. To give one pertinent example, permitting efficiencies justifications in one market to offset anticompetitive effects in a second market poses real risks of this kind. Antitrust enforcers may be strongly tempted to protect mergers having anticompetitive effects abroad where efficiencies will be realized by domestic firms. In such scenarios antitrust law can be corrupted to serve as a vehicle for externalizing costs of mergers and promoting national interests. To be sure, such risks are present in applying other aspects of merger analysis. However, where doctrine is ill-defined, the corrective pressures of international scrutiny may not be as effective.

A second consequence of an expanded efficiencies defense is the likelihood of a "race to the bottom" among antitrust authorities. Faced with the prospect of being seen as applying an overly-restrictive efficiencies test as compared to that of other competition authorities, enforcers may well conclude that the best policy is a lenient policy. Such perceptions can easily ratchet antitrust standards downward, as a kind of Gresham's Law fosters dilution of enforcement involving mergers with an international dimension. Even if national authorities avoided this downward spiral, deference to each others' judgments in merger cases would be less likely. Given the lack of transparency in efficiency analyses, second-guessing of mergers cleared by foreign authorities with greater economic interests and access to information seems inevitable. Not only would this slow progress towards harmonization of merger standards, but, by making bilateral enforcement less effective, it would also increase international frictions and encourage confrontations of the sort experienced in the McDonnell Douglas/Boeing merger.

Finally, the American experience with efficiency defense illustrates the paradox that such reviews push antitrust authorities toward imposing highly regulatory restrictions in order to assure that efficiencies are actually achieved and passed on to consumers. Restructuring, mandatory licensing, price-freezes and other edicts have become familiar remedies in settlements that allow mergers to go forward. Where efficiencies are the central issue, however, these remedies take on a decidedly intrusive flavor that may include outright supervision of rates or output. The desire of enforcement agencies to "lock in" the promised savings and ensure that consumers will benefit from them has led some American enforcement agencies and courts down a slippery slope toward outright rate regulation. In accepting highly regulatory consent agreements, these enforcers have assumed a role they are institutionally ill-equipped to perform. Applying similar remedies to international mergers would unwisely blur the line between competition policy and trade regulation and would serve to strengthen the hand of those who advocate industrial policy solutions to economic problems.

## IV. CONCLUSION

Antitrust guidelines serve the public interest when they reflect a strong consensus about appropriate antitrust policy and articulate standards that clarify the factual and legal determinations made by agencies and the courts. Where consensus and clear standards are lacking, as was the case with the Justice Department's analysis of entry barriers in the 1982 iteration of its Merger Guidelines, they may actually increase confusion and uncertainty.[110] This essay places the American efficiency defense guidelines in the latter category. The EU is best advised to stay clear of the entanglements these

110. *See* Jonathan Baker, *The Problem with* Baker-Hughes *and* Syufy: *On the Role of Entry Analysis in Merger Analysis,* 65 ANTITRUST L.J. 353 (1997); Richard Schmalensee, *Ease of Entry: Has the Concept Been Applied Too Readily?*, 56 ANTITRUST L.J. 41 (1987).

guidelines are likely to foster and thereby prevent the potential politicization of international merger reviews.