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# Merger Actions for Damages

By HERBERT HOVENKAMP\*

Mergers can have two different economic effects, one harmful to society and the other beneficial. A merger may give the post-merger firm more market power<sup>1</sup> than that enjoyed by either pre-merger firm, encouraging reduced output and higher prices for consumers.<sup>2</sup> For this reason, some mergers are illegal under the antitrust laws. Yet a merger may also benefit society by increasing the efficiency<sup>3</sup> of the post-merger firm. Increased efficiency generally results in lower costs and lower consumer prices. Even these efficiency gains cause private injuries, however, and may yield antitrust lawsuits for damages.

The very idea of a private damages action for an illegal merger is problematic. Perhaps for this reason, most actions challenging mergers under section 7 of the Clayton Act<sup>4</sup> historically have been brought by either the Federal Trade Commission (FTC) or the Department of Justice (DOJ).<sup>5</sup> The substantive law of mergers strongly suggests that these public agencies are the optimal enforcers of section 7. Section 7 is an "incipiency" statute. It was designed to nip in the bud not merely mergers that create immediate market power, but also mergers that may do so at some future time.<sup>6</sup> A perplexing, ongoing problem of

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1. Market power means the power to restrict output in the market to less than the pre-merger level and to make a profit by doing so.

2. See generally H. HOVENKAMP, *ECONOMICS & FEDERAL ANTITRUST LAW* §§ 1.2-1.3 (1985).

3. As the term is used here, a change is "efficient" if the amount gained by all who gain from the change is greater than the amount lost by all those who lose. For a discussion of efficiency and antitrust policy, see R. POSNER, *THE ECONOMICS OF JUSTICE* 92 (1981); Hovenkamp, *Distributive Justice and the Antitrust Laws*, 15 GEO. WASH. L. REV. 1, 8-12 (1982).

4. 15 U.S.C. § 18 (1982).

5. In recent years there have been about as many private filings as there have been filings by the DOJ and the FTC. See A.B.A. ANTITRUST SECTION, *MERGERS AND THE PRIVATE ANTITRUST SUIT: THE PRIVATE ENFORCEMENT OF SECTION 7 OF THE CLAYTON ACT, POLICY AND LAW* 43, 106-12 (1977) [hereinafter cited as A.B.A. ANTITRUST SEC.].

6. See *Brown Shoe v. United States*, 370 U.S. 294, 317 (1962) (stating that the 1950 Celler-Kefauver amendments to § 7 were a "provision of authority for arresting mergers at a time when the trend to a lessening of competition . . . was still in its incipency . . . , before it gathered momentum").

antitrust policy is whether private plaintiffs should have the power to enforce such a statute and, if so, whether they should have the benefit of this same "incipiency" test. Importantly, if an action in such a case involves a claim for damages, what pecuniary injury can the plaintiff show? For example, in the big Warren Court horizontal merger cases, such as *Brown Shoe*<sup>7</sup> and *Von's Grocery*,<sup>8</sup> the government presented no credible argument that these mergers, which created firms with market shares of roughly 5% to 8%, permitted the defendants to reap monopoly profits. Instead, the Court relied on a "trend" toward concentration which, if allowed to continue, might eventually produce firms with market power.<sup>9</sup> In such cases a private plaintiff clearly cannot show damages based on a post-merger monopoly overcharge. At best there is only a threat of future monopoly pricing if the merger trend continues. Perhaps private plaintiffs in such cases can show a different kind of pecuniary injury, but then a court should consider whether section 7 is the best mechanism for dealing with such claims.

These concerns once led some federal courts to conclude that there should be no private damages action for violations of section 7.<sup>10</sup> Today, however, courts routinely permit such actions.<sup>11</sup> The current in-

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7. *Brown Shoe v. United States*, 370 U.S. 294 (1962).

8. *United States v. Von's Grocery Co.*, 394 U.S. 270 (1966).

9. *Id.* at 277-78; *Brown Shoe*, 370 U.S. at 346. See also *United States v. Pabst Brewing Co.*, 384 U.S. 546 (1966) (condemning a horizontal merger creating a post-merger firm with less than 6% of the market).

10. See, e.g., *Highland Supply Corp. v. Reynolds Metals Co.*, 327 F.2d 725, 728 n.3 (8th Cir. 1964); *Bailey's Bakery, Ltd. v. Continental Baking Co.*, 235 F. Supp. 705, 717 (D. Hawaii 1964), *aff'd per curiam*, 401 F.2d 182 (9th Cir. 1968), *cert. denied*, 393 U.S. 1086 (1969). But see *Kirihara v. Bendix Corp.*, 306 F. Supp. 72, 88 (D. Hawaii 1969).

11. See, e.g., *Calnetics Corp. v. Volkswagen of America, Inc.*, 532 F.2d 674 (9th Cir.), *cert. denied*, 492 U.S. 940 (1976); *Carlson Co. v. Sperry & Hutchinson Co.*, 507 F.2d 959 (8th Cir. 1974); *Reibert v. Atlantic Richfield Co.*, 471 F.2d 727 (10th Cir.), *cert. denied*, 411 U.S. 938 (1973); *Gottesman v. General Motors Corp.*, 414 F.2d 956 (2d Cir. 1969), *cert. denied*, 403 U.S. 911 (1971); *Dailey v. Quality School Plan, Inc.*, 380 F.2d 484 (5th Cir. 1967); see also Areeda, *Antitrust Violations Without Damage Recoveries*, 89 HARV. L. REV. 1127, 1130 n.20 (1976); A.B.A. ANTITRUST SEC., *supra* note 5, at 77. See generally Day, *Private Actions Under Section 7 of the Clayton Act*, 29 ANTITRUST L.J. 155 (1965); Graybeal, *Standing and Relief in Private Section 7 Cases*, 42 ANTITRUST L.J. 561 (1973); Kintner & Wilberding, *Enforcement of the Merger Laws by Private Party Litigation*, 47 IND. L.J. 293 (1972).

The Supreme Court has never decided whether § 7 supports a private damages action, although it appears to have so assumed. In *Minnesota Mining & Mfg. Co. v. New Jersey Wood Finishing Co.*, 381 U.S. 311 (1965), the Supreme Court considered whether the statute of limitations had been tolled in a damages action based on alleged violations of §§ 1 and 2 of the Sherman Act and § 7 of the Clayton Act. The Court held that the action could proceed; however, the presence of the Sherman Act claims meant that the Court did not need to decide the legitimacy of the § 7 claim. See also *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 489 n.15 (1977) (disapproving the plaintiff's theory of recovery but suggesting in dicta that private damages actions in merger cases are permissible).

terpretation is certainly more consistent with the language of the relevant statutes. Section 4 of the Clayton Act permits persons injured "by reason of anything forbidden in the antitrust laws"<sup>12</sup> to sue for treble damages. Because section 7 is part of the "antitrust laws," the conclusion seems inescapable that Congress intended to permit private damages actions for violations of section 7.<sup>13</sup>

Nevertheless, an unrestricted private right to damages under section 7 creates a grave risk of deterring socially useful mergers. Private parties may be motivated to sue under section 7 for injuries resulting from the efficiency effects of a merger, despite the fact that those efficiencies are beneficial to society as a whole. If the purpose of antitrust law is to maximize consumer welfare by encouraging efficiency in the production and the allocation of resources, private actions for damages under section 7 should be limited to those plaintiffs who are injured by

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12. 15 U.S.C. § 15 (1982).

13. See *Heattransfer Corp. v. Volkswagenwerk, A.G.*, 553 F.2d 964, 989 n.21 (5th Cir. 1977), *cert. denied*, 434 U.S. 1087 (1978) ("We see no escape from the logic that § 7 of the Clayton Act is an antitrust statute within the scope and meaning of § 4 of the Act and so hold.") (quoting *Dailey v. Quality School Plan, Inc.*, 380 F.2d 484, 488 (5th Cir. 1967)).

Had Congress desired to deny private parties actions for damages under § 7, it could have done so. One alternative to a private damages action is the private plaintiff's right to an injunction under § 16 of the Clayton Act, 15 U.S.C. § 26 (1982). Although a merger may create no immediate market power but only the prospect of future market power, § 16 explicitly provides for private injunctive relief "against threatened loss or damage by a violation of the antitrust laws, including section . . . [7] of this title." Private injunctive relief raises serious difficulties, however, if the merger has already occurred. In such a situation, the private plaintiff normally seeks divestiture, that is, a judicially mandated restructuring of the market. A post-merger divestiture often yields only a very poor approximation of pre-merger market conditions. See *Gulf & Western Indus., Inc. v. Great Atl. & Pac. Tea Co.*, 356 F. Supp. 1066, 1074 (S.D.N.Y.), *aff'd*, 476 F.2d 687 (2d Cir. 1973) (temporary injunction less burdensome than potential future divestiture); *In re Hooker Chem. Corp.*, 59 F.T.C. 254 (1961) (parties entered into a consent order to cease and desist and to divest); see also Elzinga, *The Antimerger Law: Pyrrhic Victories?*, 12 J.L. & ECON. 43 (1969) (concluding that divestiture orders should be thorough in order to effectuate the policies of antimerger law); Pfunder, Plaine & Whittemore, *Compliance with Divestiture Orders Under Section 7 of the Clayton Act: An Analysis of the Relief Obtained*, 17 ANTITRUST BULL. 19 (1972) (questioning the effectiveness of divestiture as a remedy).

The circuit courts are split on the issue of whether divestiture is available as a private remedy in a case brought under § 7 of the Clayton Act. Compare *International Tel. & Tel. Corp. v. General Tel. & Tel. Corp.*, 518 F.2d 913, 920 (9th Cir. 1975) (remedy not available), with *Julius Nasso Concrete Corp. v. Dic Concrete Corp.*, 467 F. Supp. 1016, 1025 (S.D.N.Y. 1979) (remedy available); and *Credit Bureau Reports, Inc. v. Retail Credit Co.*, 358 F. Supp. 780, 797 (S.D. Tex. 1971), *aff'd*, 476 F.2d 989 (5th Cir. 1973) (remedy available). See generally Peacock, *Private Divestiture Suits under Section 16 of the Clayton Act*, 48 TEX. L. REV. 54 (1969) (concluding remedy should be available); Note, *The Use of Divestiture in Private Antitrust Suits*, 43 GEO. WASH. L. REV. 261 (1974) (concluding remedy should be available).

The Supreme Court's most explicit discussion of the issue is ambiguous. See *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 491 (1977).

the post-merger firm's increased market power, and should not be given to those who are injured solely by the firm's increased efficiency.

This Article examines the relationship between the public and the purely private injuries that can be caused by illegal mergers. It analyzes the efficiency defense as a means of limiting private actions to cases in which the plaintiff is injured by the market power effects of a merger. Such a defense would permit the defendant to show that the efficiency effects of a particular merger outweigh the market power effects and therefore provide a net benefit to society. The author concurs with other commentators that in most marginally illegal mergers<sup>14</sup> increased efficiencies are likely to outweigh any increase in market power. The author concludes, however, that the efficiency defense is impracticable because both the efficiency and market power effects of a merger are virtually impossible to quantify in any particular case. In fact, courts measure market power by only the crudest of proxies: usually the defendant's share of some relevant market.<sup>15</sup> Likewise, a court often cannot even identify the particular aspects of the merger that will yield efficiency gains, much less quantify those gains. Both market power and efficiency are, in the words of Judge Posner, "intractable subjects for litigation."<sup>16</sup>

Because the market power and efficiency effects of mergers are generally uncertain and rarely, if ever, measurable by the courts, this Article proposes an alternative method of determining whether a court should hear a private action seeking damages for an illegal merger. First, if the complaint on its face alleges injury resulting from the post-merger firm's increased efficiency, the case should be dismissed. Such a result is dictated by the Supreme Court's interpretation of section 4 of the Clayton Act in *Brunswick v. Pueblo Bowl-O-Mat, Inc.*<sup>17</sup> That interpretation requires a plaintiff to show that its injury resulted from that which makes the challenged conduct illegal.<sup>18</sup> Under section 7, the market power effects of a merger make it illegal, not its efficiency effects.

Second, if the complaint alleges injury resulting from a monopoly

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14. For the purposes of this Article, a marginally illegal merger is a merger that is clearly, but slightly over the threshold for legality described in the 1984 Merger Guidelines. Department of Justice Merger Guidelines, 49 Fed. Reg. 26,823 (1984) [hereinafter cited as 1984 Merger Guidelines]. However, such a merger clearly does not produce a monopolist and may not result in actual collusion, only in the increased likelihood of collusion.

15. See H. HOVENKAMP, *supra* note 2, at §§ 3.1, 3.2.

16. R. POSNER, *ANTITRUST LAW: AN ECONOMIC PERSPECTIVE* 112 (1976).

17. 429 U.S. 477 (1977).

18. See *infra* notes 80-81 & accompanying text.

overcharge, the plaintiff should be allowed to proceed. Monopoly overcharge injuries are inherently inefficient, and allowing such a claim creates little risk of deterring socially beneficial mergers.

Finally, if the plaintiff alleges some secondary anticompetitive practice, such as an exclusionary practice, the plaintiff should be required to proceed under the antitrust laws dealing with the challenged practice. The tests developed under other provisions of the antitrust laws are specifically designed to ensure that socially beneficial activity is not condemned. Allowing plaintiffs to proceed under section 7 as well creates the risk that a court will condemn the challenged practice merely because of a recent merger, without considering the overall social impact of the practice. The Supreme Court's decision in *Brunswick* can be read to require such a limitation on private actions.

### The Economic Costs of Mergers to Non-Merging Parties

When analyzing antitrust merger policy, it is essential to distinguish between the effects of a merger on society at large and its effects on individual private parties. All mergers—horizontal, vertical, and conglomerate<sup>19</sup>—may increase or facilitate the exercise of market power by the post-merger firm<sup>20</sup> as well as create substantial efficiencies.<sup>21</sup> A merger is *socially* beneficial if the social gains that result from increased efficiency outweigh the social losses that result from increased market power. However, both increased market power and efficiency gains created by mergers can produce private injuries, regardless of whether society as a whole has been harmed. For exam-

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19. This Article uses the terms "horizontal," "vertical," and "conglomerate" in the traditional way, not the way in which they are used in the 1984 Merger Guidelines. A merger is horizontal if it involves two firms that manufacture the same product and sell it in the same geographic area. A vertical merger involves two firms that stand in a supplier-buyer relationship. A conglomerate merger is a merger that is neither horizontal or vertical. The 1984 Merger Guidelines abandon the distinction between vertical and conglomerate mergers and classify all mergers as either "horizontal" or "non-horizontal." 1984 Merger Guidelines, 49 Fed. Reg. at 26,834. For criticism of this classification system, which originated in the 1982 Merger Guidelines, see Williamson, *Vertical Merger Guidelines: Interpreting the 1982 Reforms*, 71 CALIF. L. REV. 604, 605-06 (1983).

20. A merger that does not increase the post-merger firm's market power may nevertheless facilitate the exercise of market power if the merger encourages price fixing or other forms of collusion in the post-merger market. Such collusion requires that the colluding firms collectively have substantial market power. See Landes & Posner, *Market Power in Antitrust Cases*, 95 HARV. L. REV. 937, 937-38 (1981).

21. See H. HOVENKAMP, *supra* note 2, at § 11.2. "Efficiency" is used here in the potential Pareto sense: an action is potential Pareto efficient if all those who gain from the change gain enough to compensate fully all those who lose from the change, even though they do not compensate them in fact. See Hovenkamp, *supra* note 3, at 8-12.

ple, increased market power resulting from a horizontal merger may lead to higher purchase prices resulting in higher costs for customers of the post-merger firm.<sup>22</sup> The firm's competitors, on the other hand, would generally be better off; they could either sell at a higher price themselves, or increase their own output to serve the post-merger firm's former customers who are unwilling to pay the post-merger firm's increased price.

In contrast, competitors of the post-merger firm are generally injured by increased efficiency resulting from the merger. When one firm in a market becomes more efficient it can lower its prices, making its products more attractive to customers than the products of the other firms in the same market. Competitors could lose market share or, at the extreme, be forced out of the market altogether.

Analysis of the market power and efficiency effects of vertical mergers is less complex, because vertical mergers do not often increase a firm's market power, unless the market power is itself a product of the firm's increased efficiency.<sup>23</sup> On the other hand, vertical mergers can undoubtedly improve efficiency.<sup>24</sup> The same conclusion generally applies to conglomerate mergers.<sup>25</sup>

Although both increased market power and increased efficiency can impose *private* costs on those who are not parties to the merger, generally only the exercise of market power imposes *social* costs. Efficiency created by a merger generally increases social welfare.<sup>26</sup> Fur-

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22. To a lesser extent, the customers of a firm's competitors could also be injured. When a firm exercises market power by raising prices, it creates a price "umbrella" under which its competitors can also raise their prices to a supracompetitive level. Purchasers from competitors would therefore also be injured by increased market power. It is unlikely, however, that they would have a cause of action under the federal antitrust laws. See *Mid-West Paper Prod. Co. v. Continental Group, Inc.*, 596 F.2d 573, 584-86 (3d Cir. 1979); *In re Coordinated Pretrial Proceedings in Petroleum Prods. Antitrust Litig.*, 691 F.2d 1335, 1339 (9th Cir. 1982), *cert. denied*, 104 S. Ct. 972 (1984).

23. See 4 P. AREEDA & D. TURNER, *ANTITRUST LAW* ¶ 1000, at 207 (1980); R. BORK, *THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF* 225-45 (1978); Easterbrook, *Vertical Arrangements and the Rule of Reason*, 53 *ANTITRUST L.J.* 135 (1984); Posner, *The Next Step in the Antitrust Treatment of Restricted Distribution: Per Se Legality*, 48 *U. CHI. L. REV.* 6 (1981). However, there are commentators who believe that vertical integration can enhance market power under appropriate conditions. See, e.g., Williamson, *Assessing Vertical Market Restrictions: Antitrust Ramifications of the Transaction Cost Approach*, 127 *U. PA. L. REV.* 953 (1979).

24. See R. BORK, *supra* note 23, at 226; Williamson, *Economies as an Antitrust Defense Revisited*, 125 *U. PA. L. REV.* 699, 724 (1977) [hereinafter cited as Williamson, *Antitrust Revisited*]; Williamson, *supra* note 19.

25. See Williamson, *Antitrust Revisited*, *supra* note 24, at 724.

26. See *supra* note 3. For a more detailed analysis of the social costs and benefits of mergers, see Posner, *Social Costs of Monopoly and Regulation*, 83 *J. POL. ECON.* 807 (1975);

thermore, many cases decided in the 1970's and 1980's emphasize that a primary goal of federal antitrust policy is to encourage efficient practices and to condemn certain inefficient ones.<sup>27</sup> Difficulty arises, however, because many mergers simultaneously increase the merging firms' market power *and* produce efficiencies.<sup>28</sup> The overall social welfare effects of such mergers can be uncertain.

Because the role of the DOJ and the FTC is to prevent or to redress public injuries, their merger challenges presumably are based on the conclusion that the merger is socially harmful because its efficiency effects are outweighed by the potential for increased market power. Private plaintiffs, however, sue to redress private injuries. Such injuries may be caused *either* by the increased market power or by the increased efficiency of the post-merger firm. If the cause of the injury is increased market power, it is likely that society as a whole has also been injured, and a law suit would be consistent with the principle that only socially harmful mergers should be condemned. If the cause of the injury is the increased efficiency of the post-merger firm, however, a lawsuit would tend to deter mergers that are socially beneficial. To avoid overdeterrence, courts should decline to hear private plaintiffs who have been harmed not by increased market power but by increased efficiency.

### Determining the Cause of the Private Plaintiff's Injury

A court could well presume that a marginally illegal merger in the United States today does not produce private injuries from increased market power. First, the test that has been used by the Supreme Court to scrutinize mergers under section 7 is likely to condemn a merger long before the post-merger firm has attained a market share approach-

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Williamson, *Economies as an Antitrust Defense: The Welfare Tradeoffs*, 58 AMER. ECON. REV. 18 (1968). For discussion of the divergence between private and social costs in private antitrust damages claims, see Page, *Antitrust Damages and Economic Efficiency: An Approach to Antitrust Injury*, 47 U. CHI. L. REV. 467 (1980); Note, *Rethinking Antitrust Damages*, 33 STAN. L. REV. 329 (1981).

27. See, e.g., *Broadcast Music, Inc. v. CBS*, 441 U.S. 1, 19-20 (1979); *United States v. United States Gypsum Co.*, 438 U.S. 422, 441 n.16 (1978); *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 54 (1977); *Berkey Photo, Inc. v. Eastman Kodak Co.*, 603 F.2d 263, 291 n.50 (2d Cir. 1979), *cert. denied*, 444 U.S. 1093 (1980). See generally Sullivan, *The Economic Jurisprudence of the Burger Court's Antitrust Policy: The First Thirteen Years*, 58 NOTRE DAME L. REV. 1 (1982) (arguing that the Burger Court has focused on economic efficiency to the exclusion of other considerations that should be relevant).

28. See Williamson, *Antitrust Revisited*, *supra* note 24, at 723-33. See generally Fisher & Lande, *Efficiency Considerations in Merger Enforcement*, 71 CALIF. L. REV. 1580, 1587-96 (1983). For a general discussion of the kinds of economies that can be attained by horizontal and vertical integration, see F. SCHERER, *INDUSTRIAL MARKET STRUCTURE AND ECONOMIC PERFORMANCE* 81-150 (2d ed. 1980).



ing monopoly proportions.<sup>29</sup> A marginally illegal horizontal merger is not likely to have any immediately perceptible effect on the ability of the post-merger firm to reduce output and raise prices. Second, although courts today are much more cautious about condemning mergers than they were fifteen or twenty years ago,<sup>30</sup> the DOJ's 1984 Merger Guidelines<sup>31</sup> establish a threshold of illegality that is unlikely to allow post-merger firms significant market power,<sup>32</sup> in a marginal

29. See *supra* notes 6-9 & accompanying text.

30. E.g., *United States v. Waste Management, Inc.*, 743 F.2d 976 (2d Cir. 1984).

31. 1984 Merger Guidelines, 49 Fed. Reg. 26,823 (1984).

32. The 1984 Merger Guidelines employ the Herfindahl-Hirschman Index (HHI) as a measure of market concentration. The HHI is designed to reflect the fact that market power does not vary directly with market share but increases much faster than market share increases as the market becomes more concentrated. The HHI equals the sum of the squares of the market shares of the firms in the market.

Under the 1984 Merger Guidelines, the DOJ is likely to challenge a horizontal merger in which the post-merger market concentration is above 1800 as measured by the HHI and when the merger itself increases the HHI in the market by 100 points. See 1984 Merger Guidelines, 49 Fed. Reg. at 26,831. A market with one firm having a 100% market share would have an HHI of 10,000. An atomized market comprised of thousands of competitors would have an HHI approaching zero. A highly concentrated market, with three corporations having market shares of 40%, 35%, and 25% would have an HHI of 3450. ( $40^2 + 35^2 + 25^2 = 3450$ .) For further analysis, see H. HOVENKAMP, *supra* note 2, at § 11.4; Areeda, *Justice's Merger Guidelines: The General Theory*, 71 CALIF. L. REV. 303 (1983); Calkins, *The New Merger Guidelines and the Herfindahl-Hirschman Index*, 71 CALIF. L. REV. 402 (1983). See also Fox, *The New Merger Guidelines—A Blueprint for Microeconomic Analysis*, 27 ANTITRUST BULL. 519 (1982); Miller, *The Herfindahl-Hirschman Index as a Market Structure Variable: An Exposition for Antitrust Practitioners*, 27 ANTITRUST BULL. 593 (1982).

To illustrate the mechanics of the HHI in more detail, assume a market with the following structure:

Company	Market Share
A	30%
B	20%
C	10%
D	10%
E	10%
F	5%
G to Z (fringe firms)	less than 1% each

The level of concentration according to the HHI in the pre-merger market is approximately 1930. A merger between Company B and Company F would produce a post-merger HHI of about 2130. Such a merger would clearly be subject to challenge under the 1984 Merger Guidelines. Yet most likely the new company B-F will not have substantially more market power than Company B had before the merger. See *infra* notes 68-70 & accompanying text. Company B-F still is only the second largest firm in the market and still has only a 25% market share, clearly not enough to support a case for monopolization under § 2 of the Sherman Act. See *Dimitt Agri Indus. Inc. v. CPC Int'l Inc.*, 679 F.2d 516 (5th Cir. 1982), *cert. denied*, 103 S. Ct. 1770 (1983). If a private party were to file a damages action, alleging that the merger of companies B and F violated § 7, the plaintiff would almost certainly be unable to show either the fact or amount of any monopoly overcharge. The chief rationale offered by the DOJ for condemning such a horizontal merger is that the merger would make

case a private plaintiff almost certainly could not show either the fact or amount of any monopoly overcharge.<sup>33</sup> Third, mergers are absolutely public acts. Unlike price fixing or predatory pricing, a merger today generally cannot be accomplished by secret agreement. Even the smallest mergers are generally a matter of public record, and most significant mergers are announced to the government before they take place.<sup>34</sup> Consequently, mergers do not present the kinds of "detection" problems that attend price fixing, monopolization, and various forms of attempts to monopolize. Moreover, at least one of the merging parties has generally made a reasonable calculation that the merger is legal.<sup>35</sup> A merger that would give the post-merger firm the immediate ability to raise prices to monopoly levels is improbable unless someone has made a major miscalculation, in which case either the DOJ or the FTC is likely to respond swiftly.

Other evidence suggests that mergers rarely result in private injuries from increased market power. Most private merger suits are filed by competitors or potential competitors of the merging parties, rather than by consumers. Mergers that increase market power and therefore injure society are likely to benefit competitors. After the merger, competitors will be able to increase price along with the post-merger firm or to increase output to satisfy those customers unwilling to pay the post-merger firm's higher prices. On the other hand, competitors are likely to be injured when the merger increases efficiency and therefore benefits society. The post-merger firm will be able to lower prices and increase market share at the expense of competitors who cannot match the efficiencies. In most actions brought by competitors of the post-merger firm, the presumption should be that the plaintiff was injured primarily by the post-merger firm's increased efficiency, not by its increased market power.

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tacit or express collusion much more likely than it was before the merger. The mere likelihood of price fixing, however, will not support an action for damages. The private plaintiff seeking damages on such a theory would have to prove actual collusion. In that case the fact that the price fixing was facilitated by an earlier merger would be irrelevant. *See infra* note 91 & accompanying text.

33. *See supra* note 32 & accompanying text.

34. *See* Clayton Act, § 7(a), 15 U.S.C. § 18a (1982) (requiring pre-merger notification with respect to large mergers). *See generally* Symposium, *The Effects of Hart-Scott-Rodino Premerger Notification Requirements on Mergers, Acquisitions and Tender Offers*, 48 ANTITRUST L.J. 1451 (1979).

35. Both parties do not always agree as to the legality of the merger. Often the target of a hostile tender offer, for example, will oppose the merger on antitrust grounds. *See, e.g.,* Grumman Corp. v. LTV Corp., 665 F.2d 10 (2d Cir. 1981); Marathon Oil Co. v. Mobil Corp., 669 F.2d 378 (6th Cir. 1981), *cert. denied*, 455 U.S. 982 (1982). *See generally* Easterbrook & Fischel, *Antitrust Suits By Targets of Tender Offers*, 80 MICH. L. REV. 1155 (1982).

## The Failure of the Efficiency Defense

In theory, one way to avoid overdeterrence caused by a private litigant suing for injuries caused by the post-merger firm's increased efficiency is to provide the defendant with an "efficiency defense."<sup>36</sup> Under such a defense, the plaintiff would fail if the defendant proves that the socially beneficial efficiency created by the merger outweighs any harmful market power effects that the merger might also have. Unfortunately, this approach is fraught with problems.

First, it is important to consider the role that the concept of efficiency plays in antitrust policy. As a matter of history, the Supreme Court has not only condemned efficiency-creating mergers, but has sometimes condemned them precisely *because* they were efficiency-creating.<sup>37</sup> In fact, the Supreme Court has condemned mergers whose effect on the market power of the merging firms was so small that it could not be measured and whose only measurable effects were the merging firms' increased efficiency.<sup>38</sup> That position is probably no longer the law,<sup>39</sup> and today's antitrust ideology places a high value on efficiency.<sup>40</sup>

Even today, however, no general "efficiency defense" is recognized in merger cases.<sup>41</sup> Many mergers that create efficiencies are still illegal

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36. See generally Fisher & Lande, *supra* note 28; Rogers, *The Limited Case for an Efficiency Defense in Horizontal Mergers*, 58 TULANE L. REV. 503 (1983).

37. See *United States v. Von's Grocery Co.*, 394 U.S. 270 (1966); *Brown Shoe Co. v. United States*, 370 U.S. 294 (1962).

38. For example, see *Brown Shoe*, 370 U.S. at 344:

The retail outlets of integrated companies [such as the defendant], by eliminating wholesalers and by increasing the volume of purchases from the manufacturing division of the enterprise, can market their own brands at prices below those of competing independent retailers. Of course, some of the results of large integrated or chain operations are beneficial to consumers. Their expansion is not rendered unlawful by the mere fact that small independent stores may be adversely affected. It is competition, not competitors, which the Act protects. But we cannot fail to recognize Congress' desire to promote competition through the protection of viable, small locally owned business. Congress appreciated that occasional higher costs and prices might result from the maintenance of fragmented industries and markets. It resolved these competing considerations in favor of decentralization. We must give effect to that decision.

39. See *United States v. General Dynamics Corp.*, 415 U.S. 486, 497-98 (1974) (approving consideration of factors indicating that a particular merger, in fact, would not impair competition significantly even though it occurred in a moderately concentrated industry).

40. See *supra* note 27.

41. See Edwards, Joffe, Kolasky, McGowan, Mendez-Penate, Ordovery, Proger, Solomon & Toepke, *Proposed Revisions of the Justice Department's Merger Guidelines*, 81 COLUM. L. REV. 1543, 1560-64 (1981); Fisher & Lande, *supra* note 28; Muris, *The Efficiency Defense Under Section 7 of the Clayton Act*, 30 CASE W. RES. 381, 382-83 (1980); Rogers, *supra* note 36; see also Markovits, *Predicting the Competitive Impact of Horizontal Mergers in a Monopolistically Competitive World: A Non-Market-Oriented Proposal and Critique of the*

under section 7, even though the efficiencies may outweigh the undesirable market power effects. Indeed, antitrust scholars from the Chicago School,<sup>42</sup> and the 1984 Merger Guidelines,<sup>43</sup> agree that claims of specific efficiencies should not ordinarily be accepted as mitigating factors for mergers that would otherwise be challenged. The DOJ reasons as follows:<sup>44</sup> As a general rule, firms merge because the merger will either give them market power or enable them to reduce their costs.<sup>45</sup> If the merger produces no immediate market power, then the profitability of the merger must lie in its capacity to achieve certain efficiencies. Such mergers should not be condemned. However, if the merger does create a substantial threat of increased market power or collusion, then the welfare consequences of the merger can be evaluated only by balancing the social gains created by the efficiencies against any loss caused by monopoly pricing. That balancing is simply not possible except in cases where the efficiencies created by the merger are both very substantial and very obvious. For that reason the DOJ will consider post-merger efficiencies as a mitigating factor only when the merging firms produce "clear and convincing evidence" of substantial efficiencies that could not have been achieved by some other means less threatening to competition than the merger.<sup>46</sup> The efficiency statement in the 1984 Merger Guidelines—which is not really a "defense" at all, but only an indication of how the DOJ will exercise its enforcement discretion—is the closest thing to an "efficiency defense" in current merger enforcement standards.<sup>47</sup>

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*Market Definition-Market Share-Market Concentration Approach*, 56 TEX. L. REV. 587, 729-30 (1978).

42. See, e.g., R. POSNER, *supra* note 16, at 4.

43. The 1984 Merger Guidelines are a product of the new economic orientation in antitrust law, if not an outright product of Chicago School economic theories. See Schwartz, *The New Merger Guidelines: Guide to Governmental Discretion and Private Counseling or Propaganda for Revision of the Antitrust Laws?*, 71 CALIF. L. REV. 575, 577-78 (1983).

44. See Kauper, *The 1982 Horizontal Merger Guidelines: Of Collusion, Efficiency, and Failure*, 71 CALIF. L. REV. 497 (1983).

45. Of course, cost reduction itself produces market power. For example, the Landes & Posner analysis, discussed *infra* at note 65 & accompanying text, measures market power by the ratio of a firm's profit-maximizing price to its marginal costs. A firm whose marginal costs go down as a result of a merger, a patented invention, or some other efficiency-creating innovation may at least temporarily have a profit-maximizing price above its new marginal cost. The relevant question in merger cases is not whether the post-merger firm's profit rate is higher, but whether the post-merger firm has the power profitably to restrict output to below the pre-merger level.

46. 1984 Merger Guidelines, 49 Fed. Reg. at 26,834.

47. Areeda and Turner would permit an efficiency defense when both pre-merger firms in a horizontal merger suffer from substantial diseconomies because they are too small. However, they note that firms suffering from such substantial diseconomies are probably not

Even those who oppose the establishment of an "efficiency defense," however, believe that mergers have a great propensity to create efficiency, and that only a relatively small number of mergers ought to be found illegal under the antitrust laws. Indeed, if mergers contained no potential for social benefit, there would be a *per se* rule against them. In that case, any potential for harm, no matter how trivial, would justify prohibition.<sup>48</sup>

### Approaches to Balancing Efficiency and Market Price Effects: Specific Applications and General Conclusions

Although the concept of an efficiency defense has not gained much acceptance, two approaches suggest themselves as a means of preventing overdeterrence of socially beneficial mergers, and merit discussion. These approaches demonstrate that most mergers probably do create substantial efficiencies. However, analysis suggests that these approaches cannot be applied in individual cases to resolve the question of whether a particular merger should be condemned.

Professor Oliver Williamson has suggested that courts balance the market power effects of a merger against its efficiency effects.<sup>49</sup> Standing alone, this suggestion sounds much like the efficiency defense described above. However, Professor Williamson suggested that mergers produce much more substantial efficiencies than was formerly believed.<sup>50</sup> Further, he suggested that very small increases in efficiency will offset relatively large increases in market power.<sup>51</sup>

Professor Williamson first pointed out that mergers may have a greater capacity to create efficiency than antitrust lawyers and economists previously had realized. Most of this efficiency is the result of

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competitive to begin with; thus the "failing company" defense would be a more appropriate defense. 4 P. AREEDA & D. TURNER, ANTITRUST LAW 158-60 (1980).

48. . If a practice is thought to have only harmful consequences and no beneficial ones, then *per se* treatment is appropriate. See, e.g., National Soc'y of Professional Engineers v. United States, 435 U.S. 679, 692 (1978). A *per se* rule is inappropriate for mergers because a court cannot make a decision about a merger's legality until it balances the relatively ambiguous potential of the merger to increase the defendant's market power against its equally ambiguous potential to create efficiencies of production and/or distribution. See H. HOVENKAMP, *supra* note 2, at § 4.4.

49. See Williamson, *Antitrust Revisited*, *supra* note 24, at 723. The arguments appeared earlier in Williamson, *Economies as an Antitrust Defense: The Welfare Tradeoffs*, 58 AM. ECON. REV. 18 (1968) and Williamson, *The Economies of Antitrust: Transaction Cost Considerations*, 122 U. PA. L. REV. 1439 (1974).

50. Williamson, *Antitrust Revisited*, *supra* note 24, at 724.

51. *Id.* at 723.

transactional, rather than productive, economies.<sup>52</sup>

Antitrust lawyers used to look primarily at productive efficiencies, concluding that the efficiencies created by many mergers are relatively small.<sup>53</sup> As a general rule, productive economies, or economies of scale, are achieved because a larger plant or operation can function at a lower cost per unit of output than a smaller one. Often, however, mergers do not result in larger plants, but in more plants of the same size coming under the control of a single management.<sup>54</sup>

Williamson argued that the real efficiency gains from mergers result from transactional economies.<sup>55</sup> Transactional economies are economies achieved because an integrated firm needs to enter the marketplace fewer times than does a nonintegrated firm. For example, a grocer who sells potatoes must find a source of supply, negotiate a price, and bear the risk that the supplier will not perform. A grocery chain that grows its own potatoes can avoid many of these costs.

Although transactional economies are most obviously achieved by vertical mergers, horizontal mergers can facilitate them as well.<sup>56</sup> Williamson concluded that mergers for "conventional scale-economy reasons" are "much less common than mergers for transactional-economy reasons."<sup>57</sup>

Professor Williamson's more controversial conclusion was that a merger that produces "nontrivial" economies—as little as 2%—generally yields a "net allocative-efficiency gain" to society.<sup>58</sup> That is, a relatively small efficiency gain resulting from a merger would more than offset a relatively large gain in the merging firms' market power.<sup>59</sup>

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52. *Id.*

53. See, e.g., F. SCHERER, *supra* note 28, at 127-41.

54. Multi-plant economies can be substantial in certain industries, particularly if research and development costs are high, or if multi-plant operation facilitates promotion or distribution. See F. SCHERER, *supra* note 28, at 100-04; G. STIGLER, *THE ORGANIZATION OF INDUSTRY* 298-305 (1983).

55. Williamson, *Antitrust Revisited*, *supra* note 24, at 723.

56. For example, a large grocery chain can operate its own dairy or other sources of supply and thus avoid reliance on the market place. See *United States v. Von's Grocery Co.*, 384 U.S. 270, 288 (1966) (Stewart, J., dissenting).

57. Williamson, *Antitrust Revisited*, *supra* note 24, at 723. For general support of Williamson's position, see Alchian & Demsetz, *Production, Information Costs, and Economic Organization*, 62 AM. ECON. REV. 777 (1972). See also the path-breaking article by Ronald Coase, *The Nature of the Firm*, 4 *ECONOMICA* 386 (1937).

58. Williamson, *Antitrust Revisited*, *supra* note 24, at 708-09.

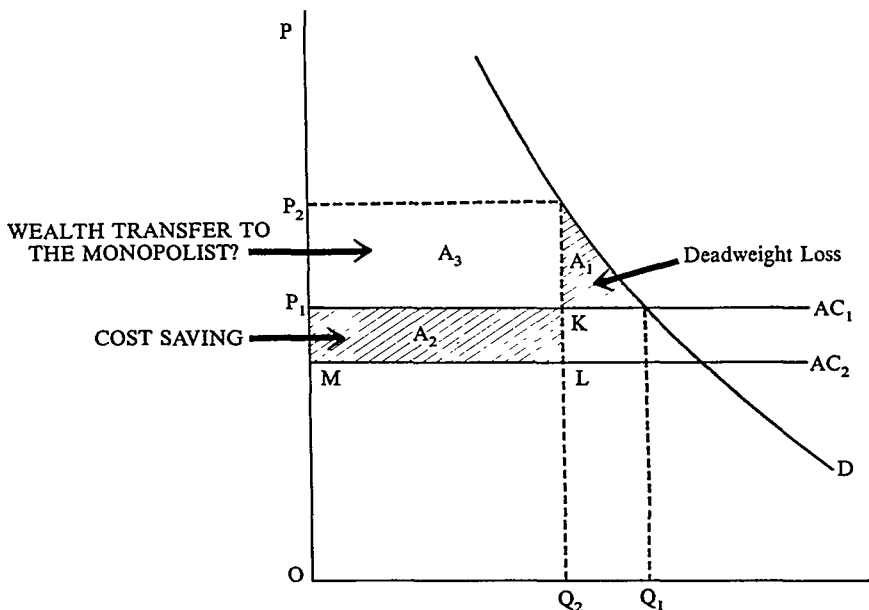
59. Figure 1 illustrates Williamson's argument. Assume that before the merger a firm had costs equal to line  $AC_1$  on the graph, but after the merger those costs were reduced to  $AC_2$ . At the same time, however, the merger gave the post-merger firm enough market power to reduce its output from  $Q_1$  to  $Q_2$ . Shaded rectangle  $A_2$  represents the efficiency gains produced by this merger, while shaded triangle  $A_1$  represents the deadweight loss pro-

Indeed, Williamson produced a table suggesting that relatively small gains in post-merger efficiency could offset relatively large price increases stemming from the post-merger firm's increased market power.<sup>60</sup>

Professor Williamson's theory is subject to some criticism. For example, although it considers the deadweight loss caused by monopoly pricing—that is, pricing in excess of marginal cost by a seller with market power—Williamson's calculations ignore the loss caused by monopoly conduct. Monopoly conduct is that conduct undertaken by a

duced by the increased market power of the post-merger firm. If the area of  $A_2$  is greater than  $A_1$ , then the merger is efficient: that is, it produces a net social gain, even though it produces a certain amount of market power as well.

FIGURE ONE



Furthermore, in many instances  $A_2$  is larger than  $A_1$ . The efficiency gains are distributed over every unit of production that the post-merger firm sells. On the other hand, the deadweight loss caused by the reduction in output applies only to the amount of output restricted. Thus, for example, if the post-merger firm was able to reduce output by 10% from the pre-merger level, the deadweight loss would be measured only over the loss suffered by those 10% of sales that are not made, and the inefficient substitutions caused thereby. On the other hand, the cost saving due to the increased efficiency will apply to the entire 90% of production remaining. See Muris, *supra* note 41, at 386.

60. Williamson, *Antitrust Revisited*, *supra* note 24, at 709.

firm in order to create or to preserve market power.<sup>61</sup> If monopoly profits are, for example, \$1,000,000 per year, a profit-maximizing firm will be willing to spend virtually any amount up to \$1,000,000, discounted by the probability of acquiring or maintaining the power, in order to acquire or keep such monopoly profits. To be sure, this money may be spent in socially beneficial ways. Research and development, for example, can yield market power to the person who comes up with a new process or invention. On the other hand, much of this money could be spent in socially detrimental ways, such as predatory pricing, false advertising, or sabotage. Economic loss to society may be caused by inefficient spending designed for no other purpose than the preservation or acquisition of monopoly power.

Another criticism of Williamson's analysis is that it permits a post-merger firm an efficiency defense even when the post-merger firm actually reduces output below the pre-merger level and charges higher prices. The firm would simply have to show that the efficiencies created by the merger outweigh the deadweight loss resulting from the monopoly pricing. It would make no difference that the benefit of these efficiencies accrued to the post-merger firm in the form of higher profits rather than to the consumers in the form of higher output and lower prices. Such an efficiency defense is inconsistent with Congress' intent and would probably be politically unacceptable.<sup>62</sup>

Professor Landes and Judge Posner have proposed an analysis that would suggest a different approach to the problem of measuring the economic effects of mergers. They have attempted to quantify the relationship between market power on the one hand and market share, market elasticity of demand, and the supply elasticity of fringe competitors on the other.<sup>63</sup> Were the necessary data available, their analysis could be used to quantify and compare any social cost incurred as a result of increased market power from a merger with the benefits resulting from efficiency gains.<sup>64</sup>

The Landes-Posner formula can be used to calculate a firm's profit maximizing price as follows:

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61. See R. POSNER, *supra* note 16, at 10-13; Posner, *The Social Cost of Monopoly and Regulation*, 83 J. POL. ECON. 807 (1975).

62. This, to be sure, is a distributive concern. See Lande, *Wealth Transfers as the Original and Primary Concern of Antitrust: The Efficiency Interpretation Challenged*, 34 HASTINGS L.J. 65, 142-45 (1982).

63. Landes & Posner, *Market Power in Antitrust Cases*, 94 HARV. L. REV. 937 (1981).

64. For similar analysis, see Schmalensee, *On the Use of Economic Models in Antitrust: The Realemon Case*, 127 U. PA. L. REV. 994 (1979).



$P_i = -C_i / (S_i / (\epsilon_m^d + \epsilon_j^s (1 - S_i)) - 1)$ ,<sup>65</sup> where:

$P_i$  = profit-maximizing price;

$C_i$  = marginal cost at price  $P_i$ ;

$S_i$  = market share;

$\epsilon_m^d$  = market elasticity of demand;<sup>66</sup> and

$\epsilon_j^s$  = the elasticity of supply of competing fringe firms.<sup>67</sup>

Assume a merger<sup>68</sup> in a market in which Company A has a 30% market share, Companies B and C have 20% each, Companies D and E have 10% each, Company F has 5%, and several small firms share the remaining 5%. Assume that the elasticity of demand in the market is 1—that is, that a 1% increase in the market price will yield a 1% reduction in demand. Finally, assume that the elasticity of supply of competing firms is 1.5—that is, that a 1% rise in price by one firm will yield a 1.5% increase in output by competitors.<sup>69</sup>

65. The formula used by Professor Landes and Judge Posner is as follows:  $(P_i - C_i) / P_i = S_i / (\epsilon_m^d + \epsilon_j^s (1 - S_i))$ . Landes & Posner, *supra* note 63, at 945. The formula in the text is restated to solve for  $P_i$ .

Landes and Posner also identify an alternative formula for directly measuring market power increases in mergers. *Id.* at 972-73. However, the formula set forth in the text is better for quantifying the effects of efficiency changes on the post-merger firm's profit-maximizing price.

66. Market elasticity of demand is the elasticity of demand faced collectively by all the firms in a market. If the market elasticity of demand is 2, a 10% price increase will result in a 20% decrease in market demand. If it is 3, a 10% price increase will yield a 30% decrease in demand.

67. Elasticity of supply considers the output of competing and fringe firms when the price in a market rises. If competitors raise output by 20% in response to a firm's 10% price increase, the elasticity of supply facing the price-raising firm is 2. If competitors raise output by 30% in response to a 10% price increase, elasticity of supply is 3.

68. See *supra* note 32.

69. The calculations given here assume that market elasticities remain constant before and after the merger. A merger may change market elasticities. See Ordover, Sykes & Willig, *Herfindahl Concentration, Rivalry, and Mergers*, 95 HARV. L. REV. 1857, 1867 (1982). However, there is no reason to think that a merger of the sort described here will change elasticities substantially, since the post-merger firm's profit-maximizing price differs from the profit-maximizing price of the pre-merger firms by only 3%.

In general, elasticity of demand rises as the market becomes more concentrated and price rises. Efficiencies, however, will mitigate this tendency.

The situation with respect to elasticity of supply is more complex. In general, if the post-merger firm's profit-maximizing price is higher than the profit-maximizing prices of the pre-merger firms, the effect will be to encourage other firms to increase output and supply elasticities will rise. However, if a firm's merger partner was the firm most likely to increase output in response to a price rise, then the elasticity of supply will be reduced. An extreme example would be a market with very high entry barriers and two existing firms each capable of expanding output without limit. If the two firms were behaving competitively, each of them would face a high elasticity of supply: as soon as one raised its price the other would increase output. A merger between the two companies would reduce elasticity of supply significantly.

In general, the rationale for a legal rule against "conglomerate," or potential competi-

In this market Company B, with a 20% market share, has a small amount of market power. If its marginal cost at its profit-maximizing output is \$1.00, its profit-maximizing price will be \$1.10.

If Company B merges with Company F, the new company B-F will have a 25% market share. In that case, if Company B-F's marginal cost at the profit-maximizing output is \$1.00, its profit-maximizing price will be \$1.13.

However, if B-F's marginal cost drops to 97 cents because of increased efficiencies produced by the merger, then B-F's post-merger profit-maximizing price will be \$1.10, the same as Company B's pre-merger profit-maximizing price.

In sum, in this particular merger, a 3% gain in efficiency would roughly offset the increase in market power created by the merger. Post-merger output would be about the same as it was before the merger, and the post-merger company's profits would be roughly 3% greater per unit of output than before the merger. The merger would produce a net efficiency gain, but, at least initially, most of the benefits of that gain would accrue to the post-merger firm.<sup>70</sup>

This hypothetical merger is challengeable under the 1984 Merger Guidelines,<sup>71</sup> but the application of the Landes-Posner analysis suggests that a relatively small efficiency increase will compensate for the increase in market power.<sup>72</sup> The effect of the efficiency gain in such a

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tion, mergers is that the merger increases market power by reducing the elasticity of supply in the relevant market. See *infra* notes 121-24 & accompanying text.

70. Over the long term, however, the post-merger firm's high rate of return will attract new capital, and competition, into the industry. Then the benefit of the efficiencies will accrue to consumers.

If there were only a 1% efficiency gain, the post-merger firm's profit-maximizing price would be \$1.12. Output would be reduced slightly, purchasing consumers would be out of pocket about 2 cents per unit, and the post-merger firm's initial profits would be about 3 cents higher per unit of output. On the other hand, if there were a 5% efficiency gain, the post-merger profit-maximizing price would be \$1.08. In that instance there would be a rather large net gain, which initially would be shared by both consumers and the post-merger firm.

If market demand elasticities were higher, the effect of efficiencies is even more dramatic. At a market elasticity of demand of 4 and a market elasticity of supply of 1.5, for example, Company B with a 20% market share would have a profit-maximizing price of \$1.04. After the merger, company B-F would have a profit-maximizing price of \$1.05. In this instance, however, a 2% efficiency gain accruing from the merger would yield a post-merger profit-maximizing price of \$1.03.

71. The hypothetical is the same as that used *supra* note 32, illustrating the application of the 1984 Merger Guidelines.

72. For example, in the hypothetical discussed a 3% gain in efficiency will roughly offset the increase in market power created by the merger.

However, it is a little more difficult, using this approach, to justify Judge Bork's argu-

marginal merger may very well be to restore output to its pre-merger level while increasing the profitability of the post-merger firm. This profitability would most likely encourage new firms to enter the market or other firms already in the market to seek out the efficiencies, perhaps through merger as well. The market would then tend toward a new equilibrium in which the benefits of the increased efficiency will be translated entirely into consumers' surplus.

Unfortunately, it does not follow that courts should attempt to balance efficiency effects against market-power effects in merger cases. Although the Landes-Posner analysis might be used to calculate the change in market power created by a hypothetical merger in a hypothetical market, the difficulty of quantifying the variables in the formula for application in the real world are generally insurmountable. First, in order to determine the effect of the merger on the post-merger firm's market power, we would need to know the merging companies' market share, which in turn requires us to define a relevant market.<sup>73</sup> Perhaps as many judicial resources have been employed in this piece of guesswork as in any aspect of merger litigation.

The formula also requires a computation of the market's elasticity of demand<sup>74</sup> and the elasticity of supply of competing firms. These data are notoriously difficult evidence to acquire for any market. Technical economists laboring under the best of academic conditions have disputed elasticities over a wide range.<sup>75</sup> Almost any attempt in litiga-

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ment that horizontal mergers should not be challenged until the post-merger companies achieve market shares in excess of 60% or so. *See* R. BORK, *supra* note 23, at 221. A firm with a market share of 30% and a marginal cost at its profit-maximizing output of \$1.00, in a market with an elasticity of demand of 1 and an elasticity of supply of competing and fringe firms of 1.5, would have a profit-maximizing price of \$1.17. If the firm merged with another identical firm with no change in efficiency, the profit-maximizing price of the new firm, which has a 60% market share, would be about \$1.60. In order for such a merger to generate a post-merger profit-maximizing price equal to or less than the profit-maximizing prices of the two individual firms before the merger, the efficiency created by the merger would have to equal roughly 27%.

73. Landes and Posner suggest that precise definition of a relevant market is not critical, as long as the elasticities are computed properly for the market defined. If the market is broadly defined, the market elasticities of demand will be low. If the market is narrowly defined, elasticity of demand will be high. In general, computation of demand and supply elasticity will correct an excessively broad or excessively narrow market definition. Landes & Posner, *supra* note 63, at 947-48.

74. Both Williamson's calculations and Landes' and Posner's formula require knowledge of the elasticity of demand facing the market if market share is known, or the elasticity facing the firm if market share is not known.

75. Landes and Posner have commented on measuring elasticities of demand in real markets, when the issue was not efficiency, but computation of the percentage of a monopoly overcharge that is passed on to an indirect purchaser. *See* Landes & Posner, *Should Indirect*

tion to determine the effect of a particular merger on the post-merger firm's profit-maximizing price would involve a great deal of speculation.

Measurement of the effects of a merger on the post-merger firm's efficiency is nearly as difficult. Relevant efficiency gains are generally measured by the decrease in marginal cost for a given level of output. For example, in both the Williamson analysis and the Landes and Posner analysis discussed above, a firm producing X units per day at a marginal cost of 90 cents is 10% more efficient than a firm producing X units per day at a marginal cost of \$1.00. Unfortunately, marginal cost is not much easier to compute in litigation than the relevant elasticities of supply and demand are. Two decades of experience in predatory pricing cases have taught us that courts are not good estimators of such factors.<sup>76</sup>

On the one hand, our knowledge that relatively small efficiencies will often compensate for relatively substantial gains in market power is secure. This tells us that many mergers make society better off. On the other hand, precise balancing of efficiency gains and losses in a particular merger case is virtually impossible, particularly in litigation.<sup>77</sup>

Unless these elusive data are available, it is unrealistic to think that courts can balance the increase in the defendants' market power as

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*Purchasers Have Standing to Sue Under the Antitrust Laws? An Economic Analysis of the Rule of Illinois Brick*, 46 U. CHI. L. REV. 602, 619-20 (1979).

For other discussions of the problem of empirical determinations of elasticities, see W. BAUMOL, *The Empirical Determination of Demand Relations*, in *ECONOMIC THEORY AND OPERATIONS ANALYSIS* (1965); Schmalensee, *supra* note 64, at 1007; Working, *What Do Statistical Demand Curves Show?*, 41 Q. J. ECON. 212 (1927).

For a slightly more confident assessment of judicial ability to ascertain market elasticities in litigation, see Harris & Sullivan, *Passing on the Monopoly Overcharge: A Comprehensive Policy Analysis*, 128 U. PA. L. REV. 269 (1979); Schaefer, *Passing-On Theory in Antitrust Treble Damage Actions: An Economic and Legal Analysis*, 16 WM. & MARY L. REV. 883 (1975). For a critique of these assessments, see Landes & Posner, *The Economics of Passing-On: A Reply to Harris and Sullivan*, 128 U. PA. L. REV. 1274 (1980).

For rough estimates of price elasticities in American markets of some everyday products, see H. HOUTHAKKER & L. TAYLOR, *CONSUMER DEMAND IN THE UNITED STATES 1929-70* (1966); E. MANSFIELD, *MICROECONOMICS: THEORY & APPLICATIONS* 133-34 (1982); Hirsch, *A Survey of Price Elasticities*, 19 REV. ECON. STUDIES 50 (1951). See generally G. STIGLER, *THE THEORY OF PRICE* 32-33, 38 (3d ed. 1966); Bishop, *Elasticities, Cross-Elasticities, and Market Relationships*, 42 AM. ECON. REV. 779 (1952).

76. For a description of some of the difficulties in measuring marginal costs, see 3 P. AREEDA & D. TURNER, *ANTITRUST LAW*, ¶ 715c, at 172-74 (1978). For the problems faced by some recent courts, see generally Hovenkamp & Silver-Westrick, *Predatory Pricing and the Ninth Circuit*, 1983 ARIZ. ST. L.J. 443.

77. R. POSNER, *supra* note 16, at 112.

a result of a merger against any efficiencies. Congress was well advised to use the words "*may* lessen competition" in section 7; it knew that courts would be involved in a good deal of speculation.

### Private Merger Enforcement: Efficiency and Antitrust Injury

Because mergers can create both productive and transactional efficiencies, and because these efficiencies often can be inferred even though they cannot be measured, courts should be careful not to condemn mergers that create efficiencies that will benefit consumers. Actions brought by the DOJ or the FTC are presumably based on considerations of the social costs and benefits of mergers. We do not have that confidence about private actions. Private plaintiffs sue in order to redress private injuries, and private injuries are as likely to be caused by the efficiency effects of mergers as by their market-power effects.<sup>78</sup> Even an efficient merger that results in enlarged output and lower prices injures some people, most generally the post-merger firm's competitors or its independent dealers. Although a general efficiency defense in merger cases is impracticable, private actions for damages can be limited in several ways to avoid overdeterrence of socially beneficial mergers.

First, courts should focus on the manner in which the plaintiff was harmed by the merger. In most private merger actions seeking damages, a court can determine rather clearly, often by merely looking at the complaint, whether the plaintiff is complaining about the post-merger firm's increased market power or its increased efficiency. If the plaintiff is alleging harm based on the efficiency created by the merger, the court should dismiss the complaint. Such a result is implicitly required by the Supreme Court's antitrust injury doctrine, as defined in *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*<sup>79</sup>

In *Brunswick* the Supreme Court held that a plaintiff could not recover damages for a section 7 violation when the alleged injury resulted from the mere continuation of its competitor in the market after the competitor was acquired by the defendant.<sup>80</sup> Justice Marshall wrote for the Court that a plaintiff in such a merger case must prove "antitrust injury," that is, injury flowing from "that which makes de-

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78. See *supra* text accompanying notes 19-26.

79. 429 U.S. 477 (1977).

80. The plaintiff alleged that its competitor would have gone out of business but for the competitor's acquisition by a much larger firm. If the competitor had gone out of business, the plaintiff would have had a much larger market share. *Brunswick*, 429 U.S. at 484.

fendants' acts unlawful."<sup>81</sup> What makes the defendant's conduct unlawful in a merger case is not the merger's tendency to increase efficiency, but its tendency to increase the defendant's market power.

Second, if the plaintiff has a bona fide claim of antitrust injury that results from the defendant's increased market power, then the court should consider whether the plaintiff's injuries resulted from monopoly pricing or from some other impermissible exercise of market power.

As a general rule monopoly pricing alone is not a violation of the antitrust laws; a firm that has become a monopolist by lawful means may charge its profit-maximizing price, even though that price may be substantially above its costs.<sup>82</sup> Moreover, a monopolist may reduce output to a level that will clear the market at the profit-maximizing price.

Monopoly pricing becomes illegal under section 2 of the Sherman Act, however, if it results from illegally created market power.<sup>83</sup> Historically, mergers that create a monopoly have been violations of section 2 of the Sherman Act.<sup>84</sup> A private plaintiff who is the victim of a monopoly overcharge resulting from an illegal merger ought to have a cause of action for damages in the amount of the overcharge.<sup>85</sup> If section 4 of the Clayton Act requires courts to allow a private damages action for violation of the antitrust laws, and if the antitrust injury doctrine requires the plaintiff to show harm resulting from the defendant's exercise of market power, this is certainly the type of case in which a plaintiff should be allowed to proceed under section 7.

But what about the private plaintiff who alleges that it has been injured in some other way by the increased market power of the post-merger firm? Such injuries do occur, but there is already an array of antitrust laws designed to deal with them. A plaintiff who claims to be injured by an exclusionary practice facilitated by the post-merger firm's increased market power has a cause of action under a statute designed to measure such activities. This would perhaps be an action for monopolization or predatory pricing under section 2 of the Sherman Act, or perhaps for exclusive dealing, reciprocity or tying under section 3 of the Clayton Act. The case law under these statutes is designed to distin-

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81. *Id.* at 489.

82. *See* *United States v. Grinnel Corp.*, 384 U.S. 563, 570-71 (1966); *Berkey Photo, Inc. v. Eastman Kodak Co.*, 603 F.2d 263, 294 (2d Cir. 1979), *cert. denied*, 444 U.S. 1093 (1980).

83. H. HOVENKAMP, *supra* note 2, at § 5.6.

84. *See, e.g.*, *Standard Oil Co. v. United States*, 221 U.S. 1 (1911); *Northern Sec. Co. v. United States*, 193 U.S. 197 (1904).

85. *See infra* notes 91-92.

guish between the efficiency-creating and efficiency-destroying effects of practices alleged to be exclusionary.

For example, private plaintiffs have occasionally complained that a merger is illegal because it enabled the defendant to engage in predatory pricing.<sup>86</sup> The plausibility of such a claim aside, the plaintiff's claim of damages must depend on proof that the defendant has actually been charging a predatory price. Because mergers have the capacity to create substantial efficiencies, a post-merger price reduction that appears predatory to a competitor may in fact reflect nothing more than the post-merger firm's increased efficiency. How does one tell the difference between a predatory price reduction and a price reduction resulting from efficiency? By asking what courts always ask in predatory pricing cases brought under section 2 of the Sherman Act: namely, whether the price was calculated to drive competitors out of the market or to discipline them, so that the defendant could charge monopoly prices later.<sup>87</sup> Thus, the plaintiff will have to make out the elements of a predatory pricing claim. If it does so, its damages will not be enlarged because in the process it proves an illegal merger as well. What some courts mistakenly have done is to reason that if the plaintiff is complaining about an unlawful merger, then the existence of the merger makes the claim of predatory pricing plausible regardless of whether the post-merger pricing was really predatory. The result is what amounts to two quite different predatory pricing tests: a rather strict one for actions brought under section 2 of the Sherman Act, and a rather liberal one, when there has been a recent merger, for actions brought under section 7 of the Clayton Act.<sup>88</sup>

The unavoidable message of *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*<sup>89</sup> is that, in order to state a cause of action, a private plaintiff must be injured by the post-merger firm's market power, not by its increased efficiency. Unfortunately, post-*Brunswick* courts have often failed to read the *Brunswick* opinion this way. Properly used in private merger cases, *Brunswick's* antitrust injury doctrine can be a superb device for dealing with private merger actions at an early stage of the proceedings. Even if a merger is presumed to be unlawful—as it would

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86. See, e.g., *Purex Corp. v. Procter & Gamble Co.*, 596 F.2d 881 (9th Cir. 1979) (discussed *infra* notes 130-40 & accompanying text).

87. See Areeda & Turner, *Predatory Pricing and Related Practices Under Section 2 of the Sherman Act*, 88 HARV. L. REV. 697 (1975).

88. See the discussion of *Purex Corp. v. Procter & Gamble Co.*, *infra* notes 130-40 & accompanying text.

89. 429 U.S. 477 (1977).

be, for example, under the doctrine of offensive collateral estoppel<sup>90</sup>—a plaintiff in a merger case should not prevail unless it shows that its own injury was caused by the defendant's market power, not by its post-merger efficiency.

The discussion that follows applies the considerations developed above to three types of mergers: horizontal, vertical, and conglomerate.

### Horizontal Mergers

The law of horizontal mergers is designed to combat two evils. One is that the merger may create a monopolist with the ability to charge monopoly prices. The second is that the merger may facilitate cartelization in the post-merger market, which now has one fewer firm and perhaps a more dominant firm than it had before the merger.<sup>91</sup>

A private plaintiff complaining about price fixing would have an action for price fixing, whether or not the merger was illegal. Assuming the price fixing could be established, an additional cause of action under section 7 would be superfluous. A purchaser complaining about the creation by merger of a monopoly should also have an action for any monopoly overcharge. Although a firm may legally be a monopolist and may legally charge its profit-maximizing price, courts have consistently held that a monopoly resulting from such a merger is itself illegal. A purchaser from such a post-merger monopolist should be allowed to bring its action under section 7 of the Clayton Act for two reasons. First, a merger that yields a price increase to monopoly levels is very likely inefficient. Second, the purchaser who pays a monopoly price has suffered the most classic kind of "antitrust injury."

Few cases brought under section 7, however, have alleged such facts.<sup>92</sup> Most private antitrust actions challenging horizontal mergers

90. A legal presumption that a merger is unlawful can arise in two ways. First, § 5(a) of the Clayton Act, 15 U.S.C. § 16(a) (1982), provides that an earlier judgment in favor of the government shall be prima facie evidence of a violation in a subsequent private action. *See* Sam Fox Publishing Co. v. United States, 366 U.S. 683, 690 (1961); *Purex Corp. v. Procter and Gamble Co.*, 453 F.2d 288, 290-91 (9th Cir. 1971), *cert. denied*, 401 U.S. 1065 (1972). Second, if the requirements are met, a determination that the defendant has violated the law in any action, whether public or private, can be dispositive with respect to a different, subsequent plaintiff under the doctrine of offensive collateral estoppel. *See* *Parklane Hosiery Co. v. Shore*, 493 U.S. 322, 331-32 (1979); *GAF Corp. v. Eastman Kodak Co.*, 519 F. Supp. 1203, 1210-12 (S.D.N.Y. 1981). *See generally* 18 C. WRIGHT, A. MILLER & E. COOPER, *FEDERAL PRACTICE AND PROCEDURE* §§ 4468-4469 (1981); Note, *Section 5(a) of the Clayton Act and Offensive Collateral Estoppel in Antitrust Damage Actions*, 85 YALE L.J. 541 (1976).

91. H. HOVENKAMP, *supra* note 2, at § 11.1.

92. *Joseph Ciccone & Sons, Inc. v. Eastern Indus., Inc.*, 537 F. Supp. 623 (E. D. Pa. 1982), may be of this variety, but it is difficult to tell from the opinion.



have been brought by the targets of tender offer bids.<sup>93</sup> Such plaintiffs cannot be victims of antitrust injury as defined by *Brunswick*, because the plaintiff will be the beneficiary, not the victim, of any market power held by the post-merger firm.<sup>94</sup> After the merger, the target will share with the tender offeror any profits generated by increased market power. The target's motives in challenging the acquisition generally have nothing to do with the antitrust consequences of the merger.

Cases have also arisen in which a distributor was terminated in the wake of an allegedly illegal horizontal merger.<sup>95</sup> Such a termination could be part of a scheme, whether monopolization or collusion, that results in reduced output by the post-merger firm. Since the post-merger firm produces less after the merger than the two merger partners did before, the post-merger firm requires fewer distributors. On the other hand, the termination could have been caused by the post-merger firm's increased efficiency; after the merger a single dealer or distributor might be sufficient to handle the output of both firms.

If the dealer is terminated because of increased efficiency, there should be no action for damages as a matter of policy. The dealer is not a victim of antitrust injury. If the termination is part of a firm's post-merger output reduction, the terminated dealer already has a cause of action for monopolization or attempt to monopolize under section 2 of the Sherman Act.<sup>96</sup> The question whether the horizontal

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93. See, e.g., *Grumman Corp. v. LTV Corp.*, 665 F.2d 10 (2d Cir. 1981); *Marathon Oil Co. v. Mobil Corp.*, 669 F.2d 378 (6th Cir. 1981), cert. denied, 455 U.S. 982 (1982).

94. See *Easterbrook & Fischel, Antitrust Suits By Targets of Tender Offers*, 80 MICH. L. REV. 1155 (1982).

95. See *John Lenore & Co. v. Olympia Brewing Co.*, 550 F.2d 495 (9th Cir. 1977). The court held that the plaintiff was not in the "target area" of the violation and dismissed the complaint for lack of standing. *Id.* at 499-500. The "target area" test is eminently ill-suited for determining whether the plaintiff's injury under such circumstances was anticompetitive. The court dismissed the plaintiff's case without deciding whether the distributor terminations were the result of efficiency or reduction of output. If the latter, the plaintiff should have had a cause of action under § 2 of the Sherman Act. The plaintiff had originally included a count under § 2 for monopolization and attempt to monopolize but later dismissed it voluntarily. *Id.* at 497 n.3. For similar use of the "target area" test, see *Solinger v. A & M Records, Inc.*, 586 F.2d 1304, 1310-12 (9th Cir. 1978), cert. denied, 441 U.S. 908 (1979); *Bosse v. Crowell, Collier & Macmillan*, 565 F.2d 602, 607 (9th Cir. 1977). See also *McDonald v. Johnson & Johnson*, 537 F. Supp. 1282, 1325-29 (D. Minn. 1982), modified, 722 F.2d 1370 (8th Cir. 1983).

96. See, e.g., *Eastman Kodak Co. v. Southern Photo Materials Co.*, 273 U.S. 359 (1927); *Photovest Corp. v. Fotomat Corp.*, 606 F.2d 704 (9th Cir. 1979), cert. denied, 445 U.S. 917 (1980); *Marquis v. Chrysler Corp.*, 577 F.2d 624 (9th Cir. 1978); see also *Dailey v. Quality School Plan, Inc.*, 380 F.2d 484 (5th Cir. 1967), *aff'd after remand*, 427 F.2d 1080 (5th Cir. 1970) (involving allegations that an employee was terminated as the result of an illegal merger); *Mount Lebanon Motors v. Chrysler Corp.*, 283 F.Supp. 453 (W. D. Pa. 1968), *aff'd*, 417 F.2d 622 (3d Cir. 1969). *Contra Reibert v. Atlantic Richfield Co.*, 471 F.2d 727 (10th

merger was illegal under section 7 has little to do with whether the dealer terminations that followed were an exercise of market power or the result of increased efficiency. The law of monopolization, not the law of mergers, is a much more suitable mechanism for addressing that question.

### Vertical Mergers

Of all mergers, vertical acquisitions are the most likely to produce efficiencies and the least likely to enhance the market power of the merging firms.<sup>97</sup> Nevertheless, private antitrust actions challenging vertical mergers have been brought under a number of theories.

Some plaintiffs have alleged simply that the new vertically integrated firm was able to undersell the plaintiff and that the plaintiff lost business as a result.<sup>98</sup> Clearly, such complaints should be dismissed under the *Brunswick* doctrine because the plaintiff is complaining that the defendant is a better competitor, not a poorer one.

In other cases, plaintiffs have alleged that a competitor's illegal vertical acquisition foreclosed the plaintiff from entering or competing in a certain market.<sup>99</sup> For example, if both plaintiff and defendant are suppliers who service a certain chain of retail stores and the defendant acquires the chain of stores, it is possible that the plaintiff will no longer supply those stores. If so, the plaintiff could be injured by the loss of business.

But is competition injured? In order to supply the retail store's requirements, the merged supplier will either have to stop supplying some other stores or increase its own output substantially. Unless the merged supplier and retail store have very large shares of their respec-

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Cir. 1972), *cert. denied*, 411 U.S. 938 (1973); *Solinger v. A & M Records, Inc.*, 586 F.2d 1304 (9th Cir. 1978), *cert. denied*, 441 U.S. 908 (1979).

97. See generally, R. BORK, *supra* note 23, at 196-201; 4 P. AREEDA & D. TURNER, ANTITRUST LAW ¶ 1000a, at 207-08 (1980).

98. This appears to be the theory under which a vertical acquisition of a supplier was challenged in *Julius Nasso Concrete Corp. v. Dic Concrete Corp.*, 467 F. Supp. 1016, 1022-23 (S.D.N.Y. 1979).

99. See, e.g., *Ohio-Sealy Mattress Mfg. Co. v. Kaplan*, 545 F. Supp. 765, 776-77 (N.D. Ill. 1982), *aff'd*, 712 F.2d 270 (7th Cir.), *cert. denied*, 104 S. Ct. 509 (1983). The plaintiff, a licensee of the defendant, alleged that it was a potential entrant into a new geographic market, but that the defendant's acquisition of a licensee in that market foreclosed the plaintiff's entry. Because the plaintiff was only a potential competitor in the market in which the acquired licensee was located, and not an actual competitor, the court decided that the plaintiff was not in the target area of the acquisition and therefore lacked standing to sue. *Id.* at 774-76. See also *Bayou Bottling, Inc. v. Dr. Pepper Co.*, 543 F. Supp. 1255 (W.D. La. 1982), *aff'd*, 725 F.2d 300 (1984) (summary judgment granted to defendant when plaintiff, alleging foreclosure, presented evidence of the increased efficiency of the post-merger defendant).

tive markets, there will be some realignment of buyers and sellers, but there will not be any foreclosure.<sup>100</sup> Furthermore, under certain circumstances the retail store may not purchase all of its requirements from the merged supplier. If the post-merger firm is a profit-maximizing firm, it will purchase from the merged supplier only if that supplier is the lowest-cost source of supply.<sup>101</sup>

*Heattransfer Corp. v. Volkswagenwerk, A.G.*<sup>102</sup> illustrates the foreclosure theory. Volkswagen acquired Delanair, a company that manufactured and supplied its dealers with automobile air conditioners.<sup>103</sup> Volkswagen's status as a monopolist (actually, a monopsonist)<sup>104</sup> was established by a jury finding that the relevant market was air conditioners for Volkswagen automobiles.<sup>105</sup> The plaintiff also manufactured air conditioners for Volkswagens. It alleged that as a result of the acquisition the defendant purchased all of its air conditioners from Delanair to the exclusion of the plaintiff.<sup>106</sup>

The foreclosure theory is most plausible when one of the merging firms is a monopolist.<sup>107</sup> Even in that case, however, it is not obvious how vertical integration can injure consumers. Volkswagen could completely foreclose other firms from the market for Volkswagen air conditioners by acquiring an air conditioning manufacturer.<sup>108</sup> But that

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100. See 4 P. AREEDA & D. TURNER, ANTITRUST LAW ¶ 1004, at 223-24 (1980). Areeda and Turner find "that the foreclosure theory has grave weaknesses." *Id.* at 221. See also R. BORK, *supra* note 23, at 231-34.

101. If all suppliers are equally efficient but the vertical merger reduces transaction costs between the two merging firms, then it would be to their advantage to deal only with each other. Such transactional economies probably explain the vast majority of vertical mergers. See O. WILLIAMSON, MARKETS AND HIERARCHIES: ANALYSIS AND ANTITRUST IMPLICATIONS 90-95 (1975); Bork, *Vertical Integration and the Sherman Act: The Legal History of an Economic Misconception*, 22 U. CHI. L. REV. 157, 195 (1954); Williamson, *Antitrust Revisited*, *supra* note 24, at 723-26.

102. 553 F.2d 964 (5th Cir. 1977), *cert. denied*, 434 U.S. 1087 (1978). See also *Calnetics Corp. v. Volkswagen of America, Inc.*, 532 F.2d 674 (9th Cir. 1976), *cert. denied*, 429 U.S. 940 (1976).

103. 553 F.2d at 974-75. Volkswagen of America, Volkswagenwerk's subsidiary in the United States, acquired Delanair. *Id.*

104. A monopsonist is a monopoly buyer.

105. 553 F.2d at 970-71, 981.

106. *Id.* at 974.

107. See H. HOVENKAMP, *supra* note 2, at §§ 7.2-7.3.

108. However, the plaintiff did not show that either Volkswagenwerk, the automobile manufacturer, or its retail dealers had any market power in automobiles generally or in air-conditioned automobiles. To be sure, a monopsonist in one market who resells as a competitor in a different market can maximize its profits by reducing output. Assume, for example, that Volkswagen sold automobiles in a competitive market at \$5,000 and that it would pay \$500 for air conditioners from independent manufacturers in a competitive market. Because Volkswagen is a monopsonist it can reduce its buying rate and obtain a lower price; perhaps

alone does not make the merger anticompetitive. As a profit-maximizing firm, Volkswagen is still motivated to deal with the most efficient producer of air conditioners, even if it happens to own a different producer.<sup>109</sup>

Regardless of whether vertical integration by a monopolist is socially detrimental, the plaintiff who is injured because its competitor was acquired by a monopolist has a cause of action under the Sherman Act.<sup>110</sup> Indeed, the plaintiff in *Heattransfer* would have suffered precisely the same injury had Volkswagen built its own air conditioning manufacturer from scratch. The determination of whether Volkswagen's vertical integration was socially beneficial or detrimental had nothing to do with the fact that the integration was carried out by means of a merger.<sup>111</sup> The plaintiff did not suffer "antitrust injury" from a section 7 violation.

Private plaintiffs conceivably might attack a vertical merger on two additional theories, provided that one of the parties to the merger

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it can then maximize its mark-up on air-conditioned automobiles by buying fewer air conditioners and selling fewer air-conditioned Volkswagens. The resulting reduction in output would produce allocative inefficiencies analogous to the consequences of monopoly. For a technical description of how monopsony works when the monopsony buyer resells in a competitive market, see J. HENDERSON & R. QUANDT, *MICROECONOMIC THEORY: A MATHEMATICAL APPROACH* 190-92 (3d ed. 1980).

Even assuming that Volkswagen was exercising monopsony power in the market for Volkswagen air conditioners before the acquisition, the tendency of the acquisition would be to restore output to the competitive level; it would not be profitable for Volkswagen to force its own subsidiary to sell to it at a less-than-competitive price. In any case, however, an exercise of monopsony power, whether by vertical integration or otherwise, is just as illegal under § 2 of the Sherman Act as an exercise of monopoly power, and a plaintiff injured by the anticompetitive consequences of such an exercise would have a cause of action, either for monopolization or for attempt to monopolize. *See, e.g., Swift & Co. v. United States*, 196 U.S. 375 (1905).

109. *See* R. BORK, *supra* note 23, at 227.

110. In *Heattransfer*, the Fifth Circuit affirmed a judgment for the plaintiff under the Sherman Act as well as under § 7 of the Clayton Act. 553 F.2d at 981-82.

111. In *Robert's Waikiki U-Drive, Inc. v. Budget Rent-A-Car Sys.*, 491 F. Supp. 1199, 1223-25 (D. Hawaii 1980), *aff'd*, 732 F.2d 1403 (9th Cir. 1984), the court dismissed a merger action because the fact of the merger was irrelevant to the injury alleged. In that case the plaintiff, in the business of renting cars, alleged that the defendant injured it by acquiring competing rental car companies and then assembling "fly-drive" packages under which passengers on Aloha Airlines could obtain rental cars at a low rate. Although the theory under which the plaintiff sued is unclear, it is likely that the defendant was using the fly-drive packages to avoid the price regulation of airline tickets. By combining the airline and rental car rates, the defendant was able to compete in an area where price regulation had set the fares higher than they would have been in a competitive market. The court dismissed the merger count for lack of a showing that the acquisition itself facilitated the fly-drive arrangements; similar arrangements could also be obtained with rental car agencies that had not been acquired by the defendant. *Id.* at 1224-25.

is a monopolist. First, the plaintiff can allege that the monopolist is using its monopoly at one distributional level to gain another monopoly at a second distributional level.<sup>112</sup> Second, the plaintiff can charge that the monopolist is making entry into the market more difficult by forcing a new entrant to enter at both distributional levels simultaneously.<sup>113</sup>

The first theory has no merit in logic or economics. A monopolist might in fact be able to use vertical integration to create a second monopoly, but unless the monopolist is price-regulated<sup>114</sup> it will not be able to extract any more monopoly profits from the two stages of distribution together than it could from one alone.<sup>115</sup> A single monopolist in a distribution chain can extract all the monopoly profits available, because the customers at the end of the chain determine the monopoly price. If the profit-maximizing retail price for shoes is \$40.00 a pair, but the marginal cost of producing them in a market in which all distribution levels are competitive is \$30.00, a single monopolist at any level will be able to extract the entire \$10.00 in monopoly profits.<sup>116</sup>

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112. See H. HOVENKAMP, *supra* note 2, at §§ 7.2-7.3.

113. See *Brown Shoe Co. v. United States*, 370 U.S. 294, 323-24 (1962); 3 P. AREEDA & D. TURNER, *ANTITRUST LAW* ¶ 725h, at 204-08 (1978); see also Note, *Refusals to Deal by Vertically Integrated Monopolists*, 87 HARV. L. REV. 1720, 1726 (1974).

114. A price-regulated firm might use vertical integration to avoid the price regulation and reap monopoly profits otherwise unavailable to it. For example, a price-regulated telephone line company might acquire telephone operating and equipment companies because it could more easily hide profits. That is, it could charge itself higher prices for the equipment and use these higher prices to create a higher base from which rates would be computed. See *Litton Sys., Inc. v. American Tel. & Tel. Co.*, 700 F.2d 785 (2d Cir.), *cert. denied*, 104 S. Ct. 984 (1983); *International Tel. & Tel. Co. v. General Tel. & Tel. Co.*, 518 F.2d 913 (9th Cir. 1975). In such a case the foreclosure argument is more plausible, particularly if the price-regulated defendant has a legal monopoly in the price-regulated market. The rate avoidance scheme gives the price-regulated monopolist a motive to buy from its subsidiary even though the subsidiary is not the most efficient seller.

115. 3 P. AREEDA & D. TURNER, *ANTITRUST LAW* ¶ 725b, at 199 (1978); R. POSNER, *supra* note 16, at 197. However, a firm might be able to use vertical integration in order to engage in price discrimination, thereby enlarging its monopoly profits. 3 P. AREEDA & D. TURNER, *ANTITRUST LAW* 201 (1978). In most cases of imperfect price discrimination, however, there is no way to predict whether the discrimination will generate higher or lower output. See J. ROBINSON, *THE ECONOMICS OF IMPERFECT COMPETITION* 201-02 (1933). Bork agrees. R. BORK, *supra* note 23, at 240. In any case, persistent price discrimination is not possible unless the discriminating seller has market power.

As Areeda and Turner note, reciprocal buying arrangements resulting from conglomerate mergers can also facilitate price discrimination. See 5 P. AREEDA & D. TURNER, *ANTITRUST LAW* ¶ 1129d, at 166-67 (1980).

116. If, however, a monopolist merges vertically with another monopolist, the result will be higher output and lower prices than existed when the two firms were independent. See 3 P. AREEDA & D. TURNER, *ANTITRUST LAW* ¶ 725c, at 200 (1978); 4 P. AREEDA & D. TURNER, *ANTITRUST LAW* ¶ 1012b, at 255-57 (1980).

The second theory, that vertical mergers may raise anticompetitive entry barriers, may be plausible in some circumstances, although commentators have expressed doubts.<sup>117</sup> Perhaps a monopolist can entrench its monopoly position by monopolizing a second link in the distribution chain. Anyone who wanted to invade the monopolist's territory would then have to enter at both levels.<sup>118</sup>

Even assuming that these theories are plausible, however, both state a cause of action under section 2 of the Sherman Act for monopolization or attempt to monopolize. If a competitor of a company acquired by a monopolist is foreclosed from the market, the results may be anticompetitive. Such anticompetitive foreclosure can only occur, however, in a market in which one of the parties to the vertical merger already has market power. In such a case, the party injured by the foreclosure has a cause of action for monopolization.<sup>119</sup> It is irrelevant whether there has been an illegal merger under section 7, because the injury would be the same whether the integration were by merger or by new entry.<sup>120</sup> The real issue is whether the foreclosure is anticompetitive. The law of monopolization, not the law of mergers, is best designed to resolve that issue.

### Conglomerate Mergers

The most serious abuses of section 7 have occurred in private actions seeking damages for illegal conglomerate mergers. Such cases are prime targets for the application of *Brunswick's* antitrust injury doctrine. Conglomerate merger actions have always been the most difficult to sustain, but courts on occasion have found antitrust violations, most generally under the "perceived potential entrant" theory.<sup>121</sup>

A merger is illegal under the perceived potential entrant theory if the merger involves a firm that was perceived by incumbents in a concentrated market to be a potential entrant.<sup>122</sup> So long as a potential

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117. See R. BORK, *supra* note 23, at 240-41 (expressing doubt about whether a monopolist can deter entry by vertical integration).

118. *Ash Grove Cement Co. v. FTC*, 557 F.2d 1368 (9th Cir.), *cert. denied*, 439 U.S. 982 (1978). See also *Freuhauf Corp. v. FTC*, 603 F.2d 345, 352 (2d Cir. 1979) (refusing to enjoin a merger under the entry barriers theory).

119. See, e.g., *Heattransfer Corp. v. Volkswagenwerk, A.G.*, 553 F.2d 964, 981-82 (5th Cir. 1977), *cert. denied*, 434 U.S. 1087 (1978).

120. See generally Note, *supra* note 113, at 1725-32 (discussing economic harm from vertical integration).

121. See, e.g., *United States v. Marine Bancorporation*, 418 U.S. 602, 625, 638-39 (1974); *Yamaha Motor Co., Ltd. v. FTC*, 657 F.2d 971 (8th Cir. 1981), *cert. denied*, 456 U.S. 915 (1982).

122. The perceived potential entrant theory is not the only theory under which conglomerate

entrant remains on the edge of the market, firms within the market presumably charge a price low enough to deter the potential entrant from entering. If the potential entrant acquires a firm already in the market, however, it no longer presents a threat and the firms within the market can raise their prices without concern about entry from that particular firm.<sup>123</sup>

The effects of a conglomerate merger under the perceived potential entrant theory more closely resemble those of a horizontal merger than those of a vertical merger. The conglomerate merger increases the collective market power of the firms already in the market by reducing the market's elasticity of supply.<sup>124</sup> In a market with a tendency toward oligopoly pricing, the prices would be higher after a merger.

If the theory is valid, a customer of the post-merger firm should have a cause of action under section 7 for the overcharge if it is able to show that it was forced to pay a monopoly price because a conglomerate merger eliminated a perceived potential entrant. There appear to be no such cases.

Competitors of the merging firm will *benefit* if the merger is illegal under the theory claimed for it. For example, if A, B, and C are oligopolists in some market whose pricing is restrained by a potential entrant, X, both B and C will benefit from X's acquisition of A. The potential entrant will be removed from the entire market, and B and C as well as the post-merger firm X-A will be able to increase their prices.

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erate mergers are challenged. Some mergers are challenged under an actual potential entrant theory. Under this theory a merger that has no immediate anticompetitive effects may nevertheless be adjudged anticompetitive in the long run if the acquiring firm could have entered the market *de novo* or by acquisition of a fringe firm in the market. This is because the merger will have precluded entry by the acquiring firm in a manner which would have rendered the market more competitive, rather than less competitive.

There have not been, and likely never will be, successful private actions under the actual potential entrant theory, although occasionally the courts have applied the theory in actions brought by the FTC. See *Yamaha Motor Co. v. FTC*, 657 F.2d 971, 980 (8th Cir. 1981), *cert. denied*, 456 U.S. 915 (1982); *Mercantile Texas Corp. v. Board of Governors*, 638 F.2d 1255, 1265 (5th Cir. 1981) (review of Federal Reserve Board order). Inherent in the theory is a concession that the merger causes no immediate anticompetitive injury.

Other conglomerate mergers have been challenged under the theory that they may facilitate reciprocal buying. See *FTC v. Consolidated Foods Corp.*, 380 U.S. 592, 594-95 (1965).

123. For a more complete description of the theory of potential competition mergers, see 5 P. AREEDA & D. TURNER, *ANTITRUST LAW* §§ 1116-1126, at 69-161 (1980); Brodley, *Potential Competition Mergers: A Structural Synthesis*, 87 YALE L.J. 1, 8-30 (1977).

124. The elimination of a likely entrant either reduces the likelihood of or increases the time in which new entry will occur in response to a non-cost-justified price increase. As the elasticity of supply goes down, the incumbents' profit-maximizing price goes up. See Landes & Posner, *supra* note 63, at 945-46.

On the other hand, if the merger increases the efficiency of the post-merger firm, allowing it to increase output and sell at a lower price, then the competitors of the merging firm will be injured by the merger, although consumers will be better off. Under such circumstances, the competitor should be foreclosed from bringing suit under section 7; the competitor has clearly not suffered antitrust injury.

In the leading Supreme Court case condemning a conglomerate merger under the perceived potential entrant theory, *FTC v. Procter & Gamble Co.*,<sup>125</sup> the acquiring firm (Procter & Gamble) was a manufacturer of various household cleaning products not including bleach, and the acquired firm (Clorox) manufactured nothing but bleach. The Supreme Court found that Procter & Gamble was a potential *de novo* entrant into the household bleach market and that its presence at the edge of the market had a competitive influence on price in the bleach market.<sup>126</sup> The acquisition eliminated that potential competition.

Justice Douglas' opinion in *Procter & Gamble* has been attacked as condemning the acquisition *because* it created certain efficiencies.<sup>127</sup> The Court condemned the merger, not because it would have increased the market price of bleach (which would injure consumers but benefit Clorox's competitors in bleach manufacturing), but because Clorox would have had the advantage of Procter & Gamble's large marketing and distribution system and quantity discounts in advertising, which would have given Clorox a cost advantage over its competitors.<sup>128</sup>

If the *Procter & Gamble* merger was condemned for this reason, then a competing bleach manufacturer in the post-*Brunswick* era should not have a damages action against either Procter & Gamble or Clorox. A private plaintiff may not complain that it was injured by the increased efficiency of the post-merger firm.<sup>129</sup>

The Ninth Circuit lost sight of *Brunswick* when it decided *Purex Corp. v. Procter & Gamble Co.*,<sup>130</sup> a private damages action that arose in the wake of the Supreme Court's divestiture order in *Procter & Gamble*. Purex, a competitor of Clorox in the sale of bleach, brought a private action for damages, alleging that it had been injured by the illegal

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125. 386 U.S. 568, 571, 572 (1967). The Supreme Court reversed the Sixth Circuit and affirmed an FTC order that Procter & Gamble divest Clorox. *Id.* at 581. Divestiture was completed in 1969. *Purex Corp. v. Procter & Gamble Co.*, 596 F.2d 881, 883 (9th Cir. 1979).

126. 386 U.S. at 577-78, 581.

127. See R. BORK, *supra* note 23, at 254-55; R. POSNER, *supra* note 16, at 118-20.

128. 386 U.S. at 579-81. See *supra* notes 79-81 & accompanying text.

129. See *supra* notes 79-81 & accompanying text.

130. 596 F.2d 881 (9th Cir. 1979).



merger of Procter & Gamble and Clorox.<sup>131</sup>

In *Purex* the plaintiff alleged that it was injured in several ways. First, *Purex* alleged that the defendant's acquisition of Clorox "reduced competition in the industry because Clorox acquired access to the vast marketing resources of Procter & Gamble, including advertising discounts, preferred media positions, market research, packaging capability and experienced personnel."<sup>132</sup> In response, the Ninth Circuit interpreted *Brunswick* to require 1) that the merger have anti-competitive effects, or that anti-competitive acts are facilitated by the merger; and 2) that the plaintiff has been injured by these effects or acts.<sup>133</sup> Then, in a particularly opaque statement, the Court concluded:

For instance, Procter's acquisition may have increased Clorox's efficiency, as the district court found, by enhancing Clorox's marketing resources and by making substantial advertising discounts available. Although such economies may be unobjectionable in isolation, they may be the basis of Section 4 liability if they serve as part of the mechanism by which an illegal merger lessens competition.<sup>134</sup>

The Ninth Circuit's statement that economies can be "the mechanism by which an illegal merger lessens competition" is absolutely inconsistent with *Brunswick* on the very point for which that case was decided. This was a complaint about more competition, not less, in the bleach industry.

Purex's theories of injury present an interesting hodge-podge, however, and deserve some analysis. For example, Purex alleged that post-merger Clorox engaged in false advertising.<sup>135</sup> However, such an allegation is irrelevant to the legality of the merger, whether or not the activity was anticompetitive. To be sure, a merger could facilitate deceptive advertising. For example, it might result in new management that has fewer scruples about misleading advertising than the old management had. But the injury is not "caused" by an illegal merger; it is not even "caused" by a change of management. It is caused by false advertising, and Purex should be required to plead accordingly.

A more interesting allegation was that after the merger Procter &

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131. *Id.* at 883. The Supreme Court's opinion in *Procter & Gamble* had foreclosed any reasonable argument that the merger itself had been legal. See *Purex Corp. v. Procter & Gamble Co.*, 453 F.2d 288, 290 (9th Cir. 1971), *cert. denied*, 405 U.S. 1065 (1972); see also *supra* note 90 (discussion of collateral estoppel).

132. 596 F.2d at 884. This allegation should have been dismissed for failure to state a claim. It appears on its face to be a complaint about the defendant's increased efficiency, not about its anticompetitive exclusionary practices. See *supra* text accompanying note 79.

133. 596 F.2d at 887.

134. *Id.* at 888.

135. *Id.* at 885.

Gamble sold Clorox bleach at a predatorily low price.<sup>136</sup> The notion that a merger can facilitate predatory pricing is questionable.<sup>137</sup> Although predatory pricing requires a deep pocket, and the resources of the acquiring firm may provide one, the merger itself has little bearing on whether predatory pricing is a rational activity in a particular instance. That determination depends upon the structure of the market in which the alleged predatory pricing takes place.<sup>138</sup>

More important, however, is the question of whether Purex was injured by predatory pricing or merely by lower prices reflecting increased efficiencies. That determination requires analysis of the relationship between the defendant's prices and its costs.<sup>139</sup> Purex also alleged that it was injured by the merger because post-merger Clorox was able to take advantage of certain production and transactional economies that were not available to the plaintiff. This allegation suggests that the efficiencies created by the merger may have enabled the defendant to lower its price. To permit recovery for an illegal merger

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136. *Id.* at 884. The district court found that Clorox did engage in "below-cost" pricing after the acquisition; however, it was "localized and temporary." *Id.* at 885.

137. *But see infra* note 138. Courts have occasionally suggested the possibility of condemning mergers on the theory that they facilitate predatory pricing. *See Reynolds Metals Co. v. FTC*, 309 F.2d 223, 229-30 (D.C. Cir. 1962); *United States v. Aluminum Co.*, 233 F. Supp. 718, 727-28 (E.D. Mo. 1964), *aff'd*, 382 U.S. 12 (1965). In general, there is little reason to believe that a firm is more likely to engage in predatory pricing after a merger than it was before. In any case, a court must analyze the relationship between the defendant's prices and costs before it can determine whether a price is predatory. *See generally* 5 P. AREEDA & D. TURNER, ANTITRUST LAW ¶ 1136, at 219-24 (1980) (discussing predatory pricing and mergers). Plaintiffs have also sometimes complained that vertical mergers facilitated predatory pricing. *See Gulf Oil Corp. v. Copp Paving Co.*, 419 U.S. 186, 211 (1974) (Douglas, J., dissenting).

138. If a market contains three firms, A, B, & C, it is easier for post-merger firm A-B to engage in successful predatory pricing against C than for A acting alone to do so against both B and C. This is true particularly if the firms are of roughly equal size. In general, a firm with a large market share can engage in predatory pricing more cheaply than can a firm with a small market share, because a proportionately smaller increase in the larger firm's output would have a proportionately larger impact on the victim. For example, if the predator has 80% of a market and the victim 20%, a 10% increase in the predator's output would reduce the victim's output by 40% (ignoring customers who enter the market at the predatory price, but who were not purchasing at all at the competitive price). On the other hand, if two firms share a market equally, a 50% increase in output by the predator would result in only a 50% decrease in sales by the victim. Before a merger would make predatory pricing significantly easier, however, the increase in market share must be substantial, much more than § 7 permits. Finally, the theory that a post-merger firm's larger market share can facilitate predatory pricing applies only to horizontal mergers. In vertical mergers and in conglomerate mergers such as Procter-Clorox, the post-merger firm does not occupy a larger share of any market than it did before, except insofar as post-merger efficiencies enable it to lower its price and increase its output.

139. *See* 5 P. AREEDA & D. TURNER, ANTITRUST LAW ¶ 1136, at 219-24 (1980).

under such a theory strikes at the heart of the antitrust injury doctrine.<sup>140</sup>

To recover for its alleged injury, the plaintiff should be required to show that the defendant's post-merger price was predatory—designed to drive rivals from the market so that the defendant could price monopolistically in the future.<sup>141</sup> In *Purex*, however, the court apparently assumed that the existence of either an illegal merger or low-priced sales made by a newly-merged company required a different analysis from the court's accepted analysis for predatory pricing.<sup>142</sup> While the Ninth Circuit has expressed its dissatisfaction with the current tests for determining whether pricing is predatory,<sup>143</sup> the court offered no reason for applying one standard to a post-merger firm and a different standard in the absence of a recent merger. The irrationality of applying a different standard is underscored by the fact that a post-merger price decrease can be expected if the merger creates substantial efficiencies. When a rival suddenly lowers its price we can infer one of three things: (1) the price was monopolistic before it was lowered; (2) the firm has found some new source of efficiency that enables it to sell at a lower price; or (3) the new price is predatory. The one significant difference between an allegation of price predation in the wake of a

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140. See *supra* notes 79-81 & accompanying text.

141. In a circuit that has adopted the Areeda-Turner test for predatory pricing, 3 P. AREEDA & D. TURNER, ANTITRUST LAW ¶¶ 709-722, at 148-94 (1980), the plaintiff would have to show that the defendant's prices were below its average variable cost. The Ninth Circuit has adopted a variation of the Areeda-Turner test for predatory pricing. See *Transamerica Computer Co. v. IBM Corp.*, 698 F.2d 1377, 1384-86 (9th Cir.), *cert. denied*, 104 S. Ct. 370 (1983); *William Inglis & Sons Baking Co. v. ITT Continental Baking Co.*, 668 F.2d 1014, 1034-36 (9th Cir. 1981), *cert. denied*, 103 S. Ct. 57 (1982); *Janich Bros. v. American Distilling Co.*, 570 F.2d 848, 857-59 (9th Cir. 1977), *cert. denied*, 439 U.S. 829 (1978); *Hanson v. Shell Oil Co.*, 541 F.2d 1352, 1358-59 (9th Cir. 1976), *cert. denied*, 429 U.S. 1074 (1977); see also *California Computer Prods., Inc. v. IBM Corp.*, 613 F.2d 727, 742-43 (9th Cir. 1979). See generally Hovenkamp & Silver-Westrick, *supra* note 76.

142. The court was ambiguous on the point. Several times the opinion refers to sales "below cost," but fails to indicate which cost figure is relevant. The Ninth Circuit remanded the case to the district court so that a more complete record could be produced, but it did not suggest a rule for evaluating the post-merger firm's "below cost" selling. *Purex Corp. v. Proctor & Gamble Co.*, 596 F.2d 881, 889 (9th Cir. 1979). On remand the district court concluded that Purex's injuries were in fact self-inflicted, *Purex Corp. v. Proctor & Gamble Co.*, 664 F.2d 1105, 1108 (9th Cir. 1981), *cert. denied*, 456 U.S. 983 (1982), and that, in any case, its profits increased steadily during the entire period in which the alleged injuries occurred. The Ninth Circuit affirmed this decision without discussing conduct standards for the post-merger firm. *Purex Corp. v. Proctor & Gamble Co.* 664 F.2d 1105 (9th Cir. 1981), *cert. denied*, 456 U.S. 983 (1982).

143. See, e.g., *Transamerica Computer Co. v. IBM Corp.*, 698 F.2d 1377, 1385-86 (9th Cir.), *cert. denied*, 104 S. Ct. 370 (1983) (court rejecting the *per se* aspects of the Areeda-Turner test).

merger and a predatory pricing allegation of the ordinary variety is that in the former the efficiency explanation comes immediately to mind, while in the latter it does not. If a merger does not yield immediate market power, we can expect it to yield certain efficiencies; lower prices may follow.<sup>144</sup>

The same considerations apply to Clorox's other promotional activities. To be sure, there may be circumstances in which the introduction of a new product or service, or of an existing product or service into a new area, may be predatory.<sup>145</sup> However, the fact that it is done shortly after a merger gives us no special reason for thinking that it is predatory and certainly no reason for applying a different test to determine if it was.

Perhaps a product extension merger such as Procter & Gamble's could facilitate certain package sales or reciprocity arrangements between Clorox and its parent company. For example, if Procter & Gamble manufactured household detergent, it might sell or promote detergent and Clorox bleach as a "package" after the merger. Such activity could injure a competitor in the market for the tied product. Section 3 of the Clayton Act,<sup>146</sup> however, is designed to measure directly the competitive effects of such product packaging and to draw the line between those arrangements that are competitive and those that are anticompetitive.<sup>147</sup> The nature of the economic analysis does not change simply because the defendant's package was facilitated by a merger. The law of tying arrangements is better designed than the law of mergers to determine whether a particular package sale is anticompetitive.<sup>148</sup>

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144. For a more reasonable, although incomplete, analysis of an allegation that a merger facilitated predatory pricing, see *Bayou Bottling, Inc. v. Dr. Pepper Co.*, 543 F. Supp. 1255, 1267-69 (W.D. La. 1982), *aff'd*, 725 F.2d 300 (5th Cir. 1984).

145. See *Transamerica Computer Co. v. IBM Corp.*, 698 F.2d 1377 (9th Cir.), *cert. denied*, 104 S. Ct. 370 (1983); 3 P. AREEDA & D. TURNER, *ANTITRUST LAW* ¶ 716, at 176-78 (1978); Areeda & Turner, *Predatory Pricing and Related Practices Under Section 2 of the Sherman Act*, 88 HARV. L. REV. 697, 730-32 (1975); Ordover & Willig, *An Economic Definition of Predation: Pricing and Product Innovation*, 91 YALE L.J. 8, 22-23 (1981).

146. 15 U.S.C. § 14 (1982).

147. The plaintiff's burden is a difficult one because the vast majority of tie-ins create efficiency. See R. BORK, *supra* note 23, at 365-81; Hovenkamp, *Tying Arrangements and Class Actions*, 36 VAND. L. REV. 213, 252-58 (1983). See generally Bowman, *Tying Arrangements and the Leverage Problem*, 67 YALE L.J. 19 (1957); Burstein, *A Theory of Full-Line Forcing*, 55 NW. U.L. REV. 62 (1960); Ferguson, *Tying Arrangements and Reciprocity: An Economic Analysis*, 30 LAW & CONTEMP. PROBS. 552 (1965); Note, *Reciprocal Dealing*, 76 YALE L.J. 1020 (1967).

148. Areeda and Turner discuss at some length the potential for conglomerate mergers to facilitate tie-ins, reciprocity, and exclusive dealing. 5 P. AREEDA & D. TURNER, *ANTI-*

## Conclusion

The private damages action for illegal mergers could be abolished with little loss of integrity to the federal antitrust enforcement scheme. Section 4 of the Clayton Act, however, appears not to permit such abolition. Nevertheless, a consumer-oriented antitrust policy will approve mergers likely to be socially beneficial and condemn them only when they are likely to be socially harmful.

The line between efficient and harmful mergers is ambiguous, however, so ambiguous that no good case can be made for an "efficiency defense" or for any judicial balancing of the efficiency effects of a particular merger against its market power effects. The public enforcement agencies, the DOJ and the FTC, are required to redress public injuries. Presumably they will not challenge an ambiguous merger unless they have made some calculation that the merger is, on balance, socially harmful. A private plaintiff, however, makes no such calculation. Private persons seeking damages sue in order to redress private injuries, and both the efficiency effects and the market power effects of mergers cause private injuries.

As a result, a substantial divergence exists between the plaintiff's motive for bringing a merger action and the public policy against anticompetitive mergers. This divergence encourages unprincipled filings—that is, complaints that will remedy private injuries by causing social injuries. Condemnation of a socially beneficial merger is just as costly to society as the failure to condemn a socially harmful merger. Unprincipled filings plus the ambiguity and complexity of substantive merger law increases the likelihood of such socially harmful overdeterrance.

The solution to the problem of unprincipled private damages actions for illegal mergers lies in the 'antitrust injury' doctrine formulated

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TRUST LAW ¶¶ 1128-1139, at 162-231 (1980). In general, they conclude that the law should ignore mergers that show merely a "potential" for reciprocity, but should become involved when reciprocity actually results. *Id.* at 180. They note that the requirement in tie-in cases of a "not insubstantial" dollar volume of commerce in the tied product before condemning the tie-in is not applied in merger cases that threaten reciprocity. Thus, at least theoretically, a merger whose only anticompetitive effect was to facilitate tie-ins could be condemned, even though the dollar volume of interstate commerce involved was too small for the tie-in to be condemned under § 3 of the Clayton Act. *Id.* at 195. The upper limit on the dollar volume for this class of cases is suggested by the Supreme Court's indication that annual sales of \$60,000 are sufficient to activate § 3. *United States v. Loew's, Inc.*, 371 U.S. 38, 49 (1962). At least one district court has found sales of \$50,000 to be sufficient for § 1 of the Sherman Act. *Aamco Automatic Transmissions, Inc. v. Tayloe*, 407 F. Supp. 430, 435-36 (E.D. Pa. 1976). Whether a merger involving sales that small would be illegal under § 7 is doubtful unless the geographic market was very small.

by the Supreme Court in *Brunswick*. Here, a broadened and stronger version of that doctrine is proposed. The private antitrust plaintiff, unlike the public enforcement agencies, must show not only that a merger that is illegal under current substantive law has taken place, but in order to collect damages it must show *how* it was injured. If the private plaintiff was injured by the post-merger firm's increased efficiency, the complaint should be dismissed for failure of antitrust injury.

Further, if the plaintiff claims an injury caused by an anticompetitive post-merger practice, it becomes important to consider the nature of the practice and its relationship to the merger itself. On the one hand, the victim of an overcharge caused by a merger-to-monopoly ought to have a cause of action for its overcharge injury. On the other hand, the allegation that a merger facilitated some other kind of anticompetitive practice invariably reduces to the allegation that the merger facilitated a secondary antitrust violation. In such circumstances the ambiguous welfare effects of marginally illegal mergers dictate that the plaintiff be required to prove the facilitated secondary violation. If it can do so, then proof of an illegal merger is irrelevant, and the section 7 claim should be dismissed. If it cannot, then the inference is strong that the plaintiff has been injured by the post-merger firm's increased efficiency, and its complaint should be dismissed.

