Using Efficiencies To Defend Mergers:
The Current Legal Landscape

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The D.C. Circuit’s 2017 decision in United States v. Anthem¹ provides the most recent appellate court evaluation of the efficiencies defense to merger challenges under the federal antitrust laws. In that case, the Justice Department and 11 states sued successfully in the U.S. District Court for the District of Columbia to block the proposed merger of Anthem and Cigna, two prominent national health insurance carriers. The merging parties appealed, arguing that the trial court improperly rejected their claims that the merger would result in billions of dollars in cost-saving efficiencies, which they had asserted would outweigh any potential competitive harm from the proposed transaction. The D.C. Circuit affirmed the lower court, holding, inter alia, that the trial court had not abused its discretion in finding that the parties had failed to prove the existence of “the kind of extraordinary efficiencies necessary to offset” the anticompetitive effects of the merger.²

Judge Judith Rogers, authoring the majority opinion, also questioned whether the court could even consider efficiencies as a defense to an otherwise unlawful merger: “[I]t is not at all clear that [efficiencies] offer a viable legal defense to illegality under [Clayton Act] Section 7.”³ Then-Judge Brett Kavanaugh dissented, arguing in part that the court was required to account for claimed efficiencies. In his view, “Any suggestion to the contrary is not the law.”⁴

This article surveys the legal status of the efficiencies defense through the lens of Anthem and other recent circuit court opinions. It further provides practical considerations for developing efficiencies that a court would credit in evaluating a merger’s lawfulness.

Are Efficiencies a Recognizable Defense?
Merging parties spend significant resources analyzing potential efficiencies from a transaction, both to understand the value of the deal and to support the benefits of the deal before the antitrust agencies. The 2010 Horizontal Merger Guidelines recognize the role of efficiencies in offsetting a merger’s potential anticompetitive effects: “The Agencies will not challenge a merger if cognizable efficiencies are of a character and magnitude such that the merger is not likely to be anticompetitive in any relevant market.”⁵ Accordingly, the U.S. Department of Justice Antitrust Division and the Federal Trade Commission routinely consider efficiencies in analyzing a merger and credit efficiencies where they meet the agencies’ criteria.

¹ 855 F.3d 345 (D.C. Cir. 2017).
² Id. at 349.
³ Id. at 353.
⁴ Id. at 377 (Kavanaugh, J., dissenting).
Courts, however, sometimes view efficiencies claims through a different lens. Some opine that the Supreme Court has rejected the concept of an efficiencies defense, and although lower courts generally do give at least some consideration to efficiencies, a number of courts have expressed skepticism toward assigning any significant weight to them. To date, no case has held that the merging parties’ asserted efficiencies alone were sufficient to overcome established anticompetitive effects of a merger.

The Supreme Court, in its 1967 opinion in FTC v. Proctor & Gamble Co., stated that “[p]ossible economies cannot be used as a defense to illegality. Congress was aware that some mergers which lessen competition may also result in economies but it struck the balance in favor of protecting competition.”6 The key legal issues in the case, however, did not focus on efficiencies, and at least one leading treatise has indicated that “[t]he Court’s brief and unelaborated language cannot reasonably be taken as a definitive disposition of so important and complex an issue as the proper role of economies in analyzing the legality of a merger.”7

Nevertheless, a few appellate courts recently have cited the language in Procter & Gamble to question the legitimacy of an efficiencies defense. In addition to the Anthem case discussed here, in Saint Alphonsus Medical Center-Nampa Inc. v. St. Luke’s Health System, Ltd., the Ninth Circuit took note of “the Supreme Court’s statements” in Proctor & Gamble questioning whether a true efficiencies defense is viable under the law.8 The court expressed concern with an efficiencies defense because of the complexities it added to reviewing mergers.9 But it nonetheless decided to “assume . . . that because § 7 of the Clayton Act only prohibits those mergers whose effect may be substantially to lessen competition, a defendant can rebut a prima facie case with evidence that the proposed merger will create a more efficient combined entity and thus increase competition.”10 The Third Circuit, in FTC v. Penn State Hershey Medical Center, also questioned whether “an efficiencies defense even exists” based on Proctor & Gamble.11 It declined to take a position on the defense because it held that the merging parties could not “clearly show that their claimed efficiencies will offset any anticompetitive effects of the merger.”12

As noted above, the D.C. Circuit most recently addressed the efficiencies defense in United States v. Anthem, a decision that featured a significant debate between the majority and dissent.13 Unlike the Ninth and Third Circuits, however, the court in Anthem faced prior precedent in its circuit, FTC v. H.J. Heinz Co., which had adopted “the trend among lower courts . . . to recognize the defense.”14 The majority in Anthem criticized Heinz because it could not overrule Supreme

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6 386 U.S. 568, 580 (1967); see also United States v. Phila. Nat’l Bank, 374 U.S. 321, 371 (1963) (“We are clear, however, that a merger the effect of which ‘may be substantially to lessen competition’ is not saved because, on some ultimate reckoning of social or economic debits and credits, it may be deemed beneficial. A value choice . . . has been made for us already, by Congress when it enacted the amended § 7. Congress determined to preserve our traditionally competitive economy. It therefore proscribed anticompetitive mergers, the benign and the malignant alike, fully aware, we must assume, that some price might have to be paid.”).

7 PHILLIP E. AREEDA & HERBERT HOVENKAMP, AN ANALYSIS OF ANTITRUST PRINCIPLES AND THEIR APPLICATION ¶ 970c2 (2018).

8 778 F.3d 775, 789 (9th Cir. 2015).

9 Id. at 790.

10 Id. (internal citation and quotation marks omitted).

11 838 F.3d 327, 348 (3d Cir. 2016).

12 Id.; see also FTC v. Staples, Inc., 970 F. Supp. 1066, 1088 (D.D.C. 1997) (“There has been great disagreement regarding the meaning of this precedent and whether an efficiencies defense is permitted.”).

13 855 F.3d 345.

14 246 F.3d 708, 720 (D.C. Cir. 2001).
Court precedent.”15 It ultimately decided to follow Heinz for the principle that “efficiencies could rebut a prima facie showing” that a merger was anticompetitive, but noted that this “is not invariably the same as an ultimate defense to Section 7 illegality,” and that it would “leave for another day whether efficiencies can be an ultimate defense to Section 7 illegality.”16

In dissent, Judge Kavanaugh reasoned that intervening Supreme Court precedent in cases such as United States v. General Dynamics,17 and Continental T.V. v. GTE Sylvania Inc.,18 reflects a more modern approach to antitrust analysis focusing on consumer welfare.19 He suggested that this newer approach effectively overturned prior precedent.20 Given this change in the law and the Heinz decision, Judge Kavanaugh argued that the court “must take account of the efficiencies and consumer benefits that would result from this merger.”21 The majority disputed Judge Kavanaugh’s reliance on cases that did not address efficiencies and that did not expressly overrule Proctor & Gamble.22 They claimed that he applied “the law as he wishes it were, not as it currently is.”23

Courts expressing skepticism about the efficiencies defense have raised concerns about applying it in practice. They have noted challenges in measuring asserted efficiencies that have not yet occurred and the extent to which the merged firm would pass those efficiencies through to consumers.24 Some commentators also have questioned the need for the defense, arguing that merger-specific efficiencies likely are rare and that many companies need not rely on efficiencies to survive antitrust scrutiny because their market shares are low or they can benefit from the failing firm defense.25 In contrast, courts and commentators supporting an efficiencies defense argue that a proper goal of antitrust policy should be to determine whether a proposed merger is likely to result in lower prices, improved quality, or innovation in determining whether, on balance, it negatively impacts competition.26

The Department of Justice and the Federal Trade Commission have trended toward the latter view, accepting efficiencies as part of an integrated competitive effects analysis, though requir-

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15 855 F.3d at 354.
16 Id. at 355. Because the D.C. Circuit affirmed the district court’s ruling that any merger-specific and verifiable efficiencies did not offset anticompetitive harm, it did not need to resolve the issue.
19 Anthem, 855 F.3d 376 (Kavanaugh, J., dissenting).
20 Id. at 377 (“When the Supreme Court overrules a standard that it had previously used to resolve a particular class of case,” federal courts “must apply the new standard and reach the result dictated under that new standard.” “The ‘results reached under the old standard’ are no longer ‘binding precedent.’” (quoting BRYAN A. GARNER ET AL., THE LAW OF JUDICIAL PRECEDENT (2016)) (brackets omitted)).
21 Id. at 377.
22 855 F.3d at 354.
23 Id.
25 See, e.g., AREEDA & HOVENKAMP, supra note 7, ¶ 970d.
26 Heinz, 246 F.3d at 720 (“As the Merger Guidelines now recognize, efficiencies ‘can enhance the merged firm’s ability and incentive to compete, which may result in lower prices, improved quality, or new products’”) (citation omitted); United States v. Oracle Corp., 331 F. Supp. 2d 1098, 1174–75 (N.D. Cal. 2004) (concluding that the defendant did not present enough evidence of increased research and development to be cognizable, but did not disagree with the concept); Robert N. Rubinovitz, New Thinking on the Role of Fixed Cost Savings in Merger Analysis, ANTITRUST SOURCE, Apr. 2008, at 1, http://www.americanbar.org/content/dam/aba/publishing/antitrust_source/Apr08_Rubinovitz 4_21f.pdf (“[A]ntitrust policy needs to preserve the proper incentives for innovation that leads to dynamic efficiencies.”).
ing strict standards of proof and applying skepticism that efficiencies can carry the day when indicia of lessened competition are strong. In their 1997 revisions to the 1992 Horizontal Merger Guidelines, the agencies updated earlier guidance on efficiencies, noting that “the primary benefit of mergers to the economy is their potential to generate such efficiencies,” and indicating that the agencies “will not challenge a merger if cognizable efficiencies are of a character and magnitude such that the merger is not likely to be anticompetitive in any relevant market.”

The 2010 Merger Guidelines reiterated this position. The 2010 Merger Guidelines also make clear, however, that “efficiencies are most likely to make a difference in merger analysis when the likely adverse competitive effects, absent the efficiencies, are not great,” and that efficiencies “almost never justify a merger to monopoly or near-monopoly.” And at least some at the agencies have expressed concern that “accepting specific efficiencies defenses is fraught with difficulties,” including the ability to verify efficiencies and whether efficiencies are actually realized by the merging parties.

While the agencies have tended to assess efficiencies as part of the overall integrated competitive effects analysis, at least some courts appear to place significance on how they are treated procedurally. In a merger challenge, the government typically must make a prima facie showing that the transaction “will substantially lessen competition.” If the government makes such a showing, the burden shifts to the defendant to rebut the government’s case. “If the defendant successfully rebuts the presumption, the burden of producing additional evidence of anticompetitive effect shifts to the government, and merges with the ultimate burden of persuasion, which remains with the government at all times.” In rebutting a prima facie showing, defendants may present evidence on a variety of matters, such as weaknesses in the government’s market share data, the competitive significance of the parties, ease of entry, buyer power and sophistication, as well as efficiencies.

Courts typically consider efficiencies as part of a defendant’s rebuttal to the government’s prima facie case, but as discussed above at least some have expressed reluctance to consider an actual efficiencies defense. In theory, this distinction should make little difference, as efficiencies are weighed against evidence of anticompetitive harm in either case. In all scenarios, the government has the burden to prove that the merger is unlawful, and defendants have the burden to prove efficiencies. Yet, courts seem to place some importance on procedural considerations. As Judge Rodgers stated in Anthem, considering efficiencies as part of the rebuttal of the government’s prima facie case “is not invariably the same as an ultimate defense to Section 7 illegality.” But whether this distinction makes an actual difference remains to be seen.

28 2010 Merger Guidelines, supra note 5, § 10.
29 Id.
32 Id.
33 Id. at 983.
34 Id. at 985–89.
35 See, e.g., United States v. Aetna Inc., 240 F. Supp. 3d 1, 94–99 (D.D.C. 2017); Heinz, 246 F.3d at 720–22 (D.C. Cir. 2001); University Health, 938 F.2d at 1222.
36 855 F.3d at 355.
Regardless of whether efficiencies are a defense or a way to rebut anticompetitive effects, even those courts that question the legitimacy of the defense ultimately appear willing to assess efficiencies when analyzing a merger’s effects. In practice, however, courts rarely balance efficiencies against anticompetitive effects, at least in any quantitative sense, and “none of the reported appellate decisions have actually held that a § 7 defendant has rebutted a prima facie case with an efficiencies defense.”

Rather, courts tend to conclude either that the efficiencies are not merger-specific or verifiable, or that the merger will not harm competition and appears to generate efficiencies.

**Standard for Proving Efficiencies**

Courts usually follow the 2010 Merger Guidelines in setting the standard for proving efficiencies, requiring the merging parties to show that any claimed efficiencies are merger-specific, verifiable, and do “not arise from any anticompetitive reduction in output or service.” In addition, courts have held that if the merging firms have “high market concentration levels” they must supply “proof of extraordinary efficiencies” to rebut a prima facie case that the merger is unlawful.

Efficiencies are merger-specific if they “cannot be achieved by either company alone” or through some other means. Thus, if merging parties will prevail on an efficiencies defense they must be able to show what “can” or “could” be done by the merged entity. To be verifiable, asserted efficiencies cannot be “vague” or “speculative” and must be verifiable by “reasonable means.” The agency or court assessing claimed efficiencies may be skeptical of efficiencies determined “outside of the usual business planning process,” although merging parties often use consultants and economic experts to assess and present the efficiencies to the antitrust agency or court.

The standard for proving efficiencies is difficult to meet, given that the merging parties are forecasting into the future how their combined business will operate and the savings, innovations, and other benefits the combination will generate. More often than not, courts find that the parties failed to prove that their efficiencies are merger-specific or verifiable.

In *Anthem*, for example, the court held that Anthem’s claimed efficiencies were neither merger-specific nor verifiable. Anthem argued that rates would decrease and quality would improve as

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37 *St. Luke’s*, 778 F.3d at 789. We have similarly found no cases holding that efficiencies alone rebut the government’s prima facie case. See infra note 38.

38 Compare *University Health*, 938 F.2d at 1223–24 (holding that appellants could not rely on an efficiencies defense “because they failed to demonstrate that their proposed acquisition would yield significant economies”), and *United States v. H&R Block, Inc.*, 833 F. Supp. 2d 36, 89–92 (D.D.C. 2011) (finding claimed efficiencies were not merger-specific and verifiable), with *FTC v. Arch Coal Inc.* 329 F. Supp. 2d 109, 158–59 (D.D.C. 2004) (denying preliminary injunction to prevent merger based on failure to show a likelihood of demonstrating a substantial lessening of competition and also finding that while defendants failed to prove a specific amount of cognizable efficiencies, the merger would create some efficiencies that “provide[d] some limited additional evidence to rebut the claim of post-merger anticompetitive effects”), and *United States v. Carilion Health Sys.*, 707 F. Supp. 840, 842, 849 (W.D. Va.), aff’d, 892 F.2d 1042 (4th Cir. 1989) (denying challenge to merger because of failure to show anticompetitive effects and also noting efficiencies).

39 2010 Merger Guidelines, supra note 5, § 10.

40 *Heinz*, 246 F.3d at 720; see also *Anthem*, 855 F.3d at 364; *University Health*, 938 F.2d at 1223; 2010 Merger Guidelines, supra note 5, § 10.

41 *Heinz*, 246 F.3d at 722; 2010 Merger Guidelines, supra note 5, § 10.

42 Note that in *Anthem* the merging parties criticized the district court because it did not assess the “likelihood” of achieving the efficiencies and instead required certainty, 855 F.3d at 356. But the court focused on the fact that it is what Anthem “can” or “could” achieve.

43 2010 Merger Guidelines, supra note 5, § 10; *Anthem*, 855 F.3d at 359 (quoting the Merger Guidelines for the verifiability standard).

44 2010 Merger Guidelines, supra note 5, § 10.
the companies’ combined the best of both parties and rebranded products under the Anthem brand. The majority concluded, however, that Anthem could obtain any quality benefits on its own by implementing better marketing and better products. In contrast, Judge Kavanaugh reasoned that “enhanced bargaining power is a large part of what would enable Anthem-Cigna to negotiate the lower provider rates that in turn would lead to cost savings for employers,” and that this “is a direct result of the merger.”

The majority further took issue with the speculative nature of the claimed efficiencies. Anthem argued that it could apply its provider rates to Cigna customers after the merger. The court noted, however, testimony from Anthem’s CEO that the company would not immediately lower rates because it could hurt its provider relationships. It also noted the fact that providers could terminate agreements with 90 days’ notice. Thus, the court was skeptical that Anthem would achieve the claimed efficiencies.

Judge Kavanaugh viewed Anthem’s efficiencies more favorably. He stated that to be verifiable, the efficiencies “need not be certain. They merely must be probable.” He pointed to the work done by the merging parties’ economist, integration planning team, and third-party consultants, and credited the claimed savings to be between $1.7 and $3.3 billion annually, which, according to Kavanaugh, “would be largely passed through to employers (as the contracts and basic structure of this self-insured market require).”

As the majority did in Anthem, courts test efficiencies rigorously and hesitate to give the merging parties the benefit of the doubt. Merger challenges necessarily involve hypotheticals as the key question is whether the merger—an event that typically has not yet occurred—will likely lead to a substantial lessening of competition in the future. When it comes to determining anticompetitive effects, courts focus on “probabilities, not certainties or possibilities.” Yet when dealing with efficiencies, courts seem to require more. This reflects a balance that favors erring on the side of avoiding consumer harm in close calls.

Key Considerations Regarding the Efficiencies Defense

While the state of the efficiencies defense remains unsettled, some things are clear. Despite Supreme Court precedent that has questioned the efficiencies defense and other criticism of the defense, most courts will continue to evaluate claimed efficiencies in some manner when deciding a merger challenge. This is likely in part because the antitrust agencies charged with reviewing and challenging mergers include efficiencies as a component of their analysis. The trend in the appellate and district courts is to consider efficiencies at least when deciding whether a defendant has rebutted the plaintiff’s prima facie case that a merger is unlawful.

45 Anthem, 855 F.3d at 357-58.
46 Id. at 375 (Kavanaugh, J., dissenting).
47 Id. at 360.
48 Id. at 359.
49 Id. at 375 (Kavanaugh, J., dissenting).
50 Id.
51 See, e.g., Heinz, 246 F.3d at 720.
52 Baker Hughes, 908 F.2d at 984.
53 Amici in Anthem raised precisely this concern, that “the merger-specificity and verifiability requirements . . . place an asymmetric burden on merging parties that could doom beneficial mergers.” Anthem, 855 F.3d at 356. The majority, however, favored “the policy that consumers should not bear the loss of a competitor if the offsetting benefit could be achieved without a merger.” Id.
The Supreme Court also is likely to recognize the defense should it have the opportunity to do so. Now-Justice Kavanaugh clearly supports such a defense and others on the Supreme Court have shown support for a “modern” approach to antitrust law reflected in more recent case law.54

Even as courts continue to consider efficiencies in defense of a merger, however, the merging parties are unlikely to prevail on efficiencies where a court finds the merger is otherwise deemed likely to have significant anticompetitive effects.55 In addition, the bar to successfully proving efficiencies will remain high. Merging parties should ensure that asserted efficiencies are likely to be achieved given business realities and past experiences. Where contractual terms, customer or supplier relationships, or actual business plans call into question efficiencies that a party wants to assert before the antitrust agencies or a court, the parties should re-evaluate those efficiencies and ensure they are consistent with the evidence. When quantifying efficiencies, the company or an outside consultant also should use conservative estimates based on cost savings that are most likely to occur and are supported by clear ordinary course documentation. The parties should expect rigorous testing of their asserted efficiencies given that the agencies and courts will err in favor of protecting consumers against potential harm rather than assuming potential efficiencies will result in cost savings passed onto them.


55 Aetna Inc., 240 F. Supp. 3d at 94–95 (Despite Aetna and Humana implementing an “integration management office” that performed a detailed analysis through functional teams, third-party consultants, an expert at trial, and a prior acquisition where Aetna obtained efficiencies, the district court was unpersuaded “that the efficiencies generated by the merger will be sufficient to mitigate the transaction’s anticompetitive effects for consumers in the challenged markets.”); Penn State Hershey Medical Center, 838 F.3d at 349–50 (Despite the district court finding that the efficiencies offset any harm, and the circuit court concluding the capital savings are cognizable (Hershey would not have to build $277 million dollar bed tower), the circuit court concluded that the efficiencies were “insufficient to rebut the presumption of anticompetitiveness.”).