Maximizing Efficiencies: Getting Credit Where Credit Is Due

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Efficiencies are frequently a significant part of the business rationale for a transaction. However, receiving credit for the efficiency-enhancing aspects of a combination in a merger review is often difficult. By the Federal Trade Commission and Department of Justice's own account, "the antitrust laws give competition, not internal operational efficiency, primacy in protecting customers" and "efficiencies are most likely to make a difference in merger analysis when the likely adverse competitive effects, absent the efficiencies, are not great."[1] Recent transactions, such as H&R Block/Tax Act, AT&T/T-Mobile, and OSF Healthcare/Rockford, continue to confirm that receiving credit for efficiencies is no easy task.

Either because the agencies and courts have tended to set the bar very high or because efficiencies are notoriously difficult to quantify, some rightfully may ask whether merging parties should save the time and effort required to prepare a robust efficiencies argument in favor of focusing on the potentially dispositive issue of market definition and attacking theories of competitive harm. Efficiencies, however, should not be abandoned despite the challenges in demonstrating them. Indeed, a 2009 FTC study demonstrated that the agencies do examine efficiencies—the FTC's Bureau of Competition staff memoranda analyzed efficiencies in 37 of the 48 closed investigations and in 61 of the 121 consent decree cases over a ten-year period.[2] Similarly, efficiencies are touted as a rationale in many closing statements and thus can help the agencies justify clearance decisions.[3] Thus, forgoing an efficiencies argument when one exists can be costly. But given the burdens of developing substantiated efficiencies, it is critical for the parties to focus their efforts in the right areas.

The Role of Efficiencies in Merger Analysis

The "principal analytical techniques, practices, and the enforcement policy" of the U.S. antitrust authorities regarding horizontal mergers under the antitrust law are outlined in the 2010 Merger Guidelines. These guidelines replaced the 1992/1997 Guidelines and were intended to increase "the transparency of the analytical process underlying the Agencies' enforcement decisions" and "assist the courts in developing an appropriate framework for interpreting and applying the

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1 U.S. Dep't of Justice & Fed. Trade Comm'n, Horizontal Merger Guidelines § 10 (2010) [hereinafter 2010 Merger Guidelines], *available at* http://www.ftc.gov/os/2010/08/100819hmg.pdf.

2 Malcolm B. Coate & Andrew J. Heimert, Federal Trade Commission, Merger Efficiencies at the Federal Trade Commission 1997–2007 at 14 n.31 (2009) [hereinafter 2009 FTC Efficiencies Study]. The presence of efficiencies, however, does not mean such arguments are a cure-all. Indeed, efficiencies were claimed in all 17 of the cases where the agency sought a preliminary injunction.

3 *See, e.g.*, Press Release, U.S. Dep't of Justice, Statement of the Department of Justice's Antitrust Division on Its Decision to Close Its Investigation of the Merger of Delta Airlines Inc. and Northwest Airlines Corporation (Oct. 29, 2008), *available at* http://www.justice.gov/atr/public/press_releases/2008/238849.pdf.

antitrust laws in the horizontal merger context."[4] The agencies, however, did not make any substantive changes to the analysis of efficiencies from the prior Guidelines, but rather expanded the efficiencies discussion to provide more clarity on their view regarding efficiencies. Interestingly, elsewhere in the 2010 Merger Guidelines, revisions were made that increased the ranges of Herfindal-Hirschman Index (HHI) concentration levels linked to certain presumptions about the potential for anticompetitive harm from mergers in highly concentrated markets.[5] As a result, these revisions may have potentially opened the door for a successful efficiencies argument where a merger now falls below the range and is no longer *presumed* to enhance market power.[6]

Under the 2010 Merger Guidelines, the agencies only credit those efficiencies that are "merger specific." In other words, the only efficiencies that count are those "accomplished with the proposed merger and unlikely to be accomplished in the absence of either the proposed merger or another means having comparable anticompetitive effects."[7] In terms of whether another avenue is available for the same benefits, the agencies consider only "practical" alternatives and "do not insist upon a less restrictive alternative that is merely theoretical."[8]

Moreover, in addition to being merger specific, efficiencies must be substantiated or verifiable with quantifiable measurements derived—to the maximum extent possible—from information relied on by the parties in the ordinary course of business. As some courts have stated, one "must undertake a rigorous analysis of the kinds of efficiencies being urged by the parties in order to ensure that those 'efficiencies' represent more than mere speculation and promises about post-merger behavior."[9] According to the 2010 Merger Guidelines, "[V]ague, speculative, or [other efficiencies that] cannot be verified by reasonable means"[10] will not be sufficient to receive credit. Projections developed specifically for the transaction will be viewed with particular skepticism. Rather, the agencies are most likely to credit "efficiency claims substantiated by analogous past experience."[11]

Additionally, the agencies will not credit efficiencies if there is reason to believe that benefits will not be passed on to consumers. Although some have posited that consumer benefit can be presumed once efficiencies are established as cognizable (i.e., merger specific and verifiable),[12] the agencies do not accept any such presumption. According to the 2009 FTC study, staff frequently failed to credit efficiencies in their recommendation memoranda because they concluded that the savings from the efficiencies would not be passed on to consumers.[13]

Once cognizable efficiencies are established, the agencies consider whether such efficiencies likely would be sufficient to reverse a merger's potential to harm customers in the relevant market. The burden remains on the parties to make the required demonstration. The agencies will not

[4] 2010 Merger Guidelines, *supra* note 1, § 1.

[5] *See id.* § 5.3.

[6] *See, e.g.*, D. Daniel Sokol & James A. Fishkin, *Antitrust Merger Efficiencies in the Shadow of the Law*, 64 VAND. L. REV. 45, 52 (2011).

[7] 2010 Merger Guidelines, *supra* note 1, § 10.

[8] *Id.*

[9] FTC v. H.J. Heinz Co., 246 F.3d 708, 721 (D.C. Cir. 2001).

[10] 2101 Merger Guidelines, *supra* note 1, § 10

[11] *Id.*

[12] *See* Thomas B. Leary, Fed. Trade Comm'n, An Inside Look at the *Heinz* Case (June 25, 2007), *available at* http://www.ftc.gov/speeches/leary//babyfood.shtm.

[13] 2009 FTC Efficiencies Study, *supra* note 2, at 8.

conduct a linear comparison of the magnitude of the cognizable efficiencies and the magnitude of the likely harm to competition absent the efficiencies. Instead, a greater potential for adverse competitive effects requires not only a greater showing of offsetting cognizable efficiencies, but also greater pass-through of the benefits to customers in order for the agencies to conclude that the merger will not have an anticompetitive effect in the relevant market. When the potential adverse competitive effect of a merger is likely to be particularly substantial, parties must show *extraordinarily* great efficiencies.[14]

While some courts consider efficiencies an affirmative defense, most courts have considered efficiencies a means to rebut the government's prima facie case.[15] Accordingly, courts will consider first whether an acquisition would result in anticompetitive harm in the relevant market and then whether the efficiencies can overcome the structural and statistical presumptions presented in the government's prima facie case.[16] The D.C. Circuit in *Baker Hughes* set forth the basic framework for efficiencies analysis in merger litigation:

> By showing that a transaction will lead to undue concentration in the market for a particular product in a particular geographic area, the government establishes a presumption that the transaction will substantially lessen competition. The burden of producing evidence to rebut this presumption then shifts to the defendant. 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.[17]

Receiving Credit Is Not Always Easy

Despite the potential for efficiencies to matter in litigation, in most merger cases the courts have applied stringent standards and found that the parties failed to carry their burden of demonstrating cognizable efficiencies. For example, in *Heinz*, the merging parties argued that their combination of the second and third largest competitors would result in a new entity better positioned to compete with the largest competitor. The D.C. Circuit reversed the district court's analysis under which it refused to block the transaction, finding that the efficiencies were overstated and not merger specific. For one, the variable cost savings advanced were only a small percentage of overall variable costs and so did "not necessarily translate into a significant cost advantage."[18] Moreover, the court found the claimed efficiencies of manufacturing the target's "better recipes"

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[14] 2010 Merger Guidelines, *supra* note 1, § 10.

[15] *See, e.g.*, FTC v. University Health, Inc., 938 F.2d 1206, 1222 (11th Cir. 1991); *Heinz*, 246 F.3d at 720; *see also* FTC v. Arch Coal, Inc., 329 F. Supp. 2d 109, 124 (D.D.C. 2004) ("[W]here the HHI calculation potentially . . . indicates a merger to be presumptively illegal, the factors set forth in the [Horizontal Merger Guidelines] become relevant in undertaking a more comprehensive and holistic assessment . . .[that] include: the potential competitive effects of a merger, entry analysis, *efficiencies* and failure and exiting assets.") (emphasis added). Although the D.C. Circuit in *Staples* used the phrase "affirmative defense," when considering efficiencies, the court actually considered efficiencies when assessing the competitive effects of the transaction—as opposed to after the court found that the transaction was likely to substantially lessen competition. FTC v. Staples, Inc., 970 F. Supp. 1066, 1088–90 (D.D.C. 1997).

[16] Some courts, however, apply a more flexible framework. Because, in practice, the evidence is presented all at once such that the government's prima facie case anticipates and addresses the rebuttal evidence presented by defendants, some courts analyze the government's burden and the defense's burden together. *See, e.g.*, Chi. Bridge & Iron Co. N.V. v. FTC, 534 F.3d 410 (5th Cir. 2008); Olin Corp. v. FTC, 986 F.2d 1295 (9th Cir. 1993). While not employing the burden shifting framework, these courts still appear to consider the efficiencies when assessing whether defendant's evidence rebuts the government's case that the transaction will substantially lessen competition.

[17] United States v. Baker Hughes Inc., 908 F.2d 981, 983–84 (D.C. Cir. 1990) (internal citations omitted).

[18] *Heinz*, 246 F.3d at 721.

[19] *Id.* at 721–22.

at the acquirer's more efficient plant were not shown to be merger specific because the acquirer might have invested in better recipes itself.[19]

Similarly, in *CCC Holdings*, the defendants claimed that significant cost savings would result from consolidating the parties' software on a single platform. However, the merging parties acknowledged that the integration could take as long as ten years, with ultimate success remaining uncertain. And, two financial consultants hired by one of the merging parties had calculated the merger would still result in a net loss (costs versus synergies) three years out. Thus, the court found that while efficiencies might exist, "the record [was] far from clear" and they were too "speculative and supported by little more than lawyer argument," which was insufficient to overcome the "*strong* presumption of anticompetitive effects created by large HHIs and high barriers to entry in the relevant market."[20]

In *Staples*,[21] the court detailed numerous shortcomings with the acquirer's efficiencies estimates, including:

- Efficiencies claims offered in court significantly exceeded earlier figures shown to the board and made in securities filings;
- Cost savings were not properly documented (Staples' VP of Integration admitted that backup, source, and calculations for some of the savings were entirely omitted from the analysis submitted);
- The analysis used questionable methodologies;[22]
- When testifying, Staples' VP of Integration was unable to explain the methods used to calculate many of the cost savings;
- The analysis failed to deduct certain stand-alone benefits from the efficiencies figures, thereby rendering aspects of the total calculation non-merger specific; and
- The efficiencies estimates included savings from more favorable negotiations with vendors, but failed to consider any stand-alone discounts Staples might have obtained in the ordinary course of business as it had been able to do in the past.

In *Oracle*, despite refusing to enjoin the transaction, the court found the defendant's efficiencies claims "too vague and unreliable to rebut a showing of anticompetitive effect."[23] The court emphasized that the parties' expert was unable to provide a factual basis for the various inputs in spreadsheets that detailed the cost savings and no documents explained the personal judgments on the inputs, thereby rendering the claims as "too speculative to be afforded credibility."[24]

Even when courts credit efficiencies, those efficiencies might nevertheless be insufficient to overcome the government's evidence of potential anticompetitive harm. In *FTC v. Libbey*,[25] the court found that the evidence was not sufficient to rebut the government's prima facie case, given the potential harm stemming from the already highly concentrated market for food service glass-

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[20] FTC v. CCC Holdings Inc., 605 F. Supp. 2d 26, 73–75 (D.D.C. 2009).

[21] *Staples*, 970 F. Supp. at 1090.

[22] The court noted that in calculating vendor cost savings, Staples used a sample of vendors and then extrapolated the savings across all products. However, the sample group omitted Hewlett Packard, Staples's largest vendor. Moreover, "the evidence show[ed] that Staples was not confident that it could improve its buying from Hewlett Packard" yet Hewlett Packard products received the extrapolated discount in the efficiencies analysis. *Staples*, 970 F. Supp. at 1090.

[23] United States v. Oracle Corp., 331 F. Supp. 2d 1098, 1175 (N.D. Cal. 2004).

[24] *Id.*

[25] 211 F. Supp. 2d 34, 52 (D.D.C. 2002).

ware. The parties argued that the transaction would lower prices and improve product innovation, which would allow the merged firm to compete better against foreign competition. Although these efficiencies were acknowledged by the court, they were insufficient to outweigh the potential harm.[26]

More recently, efficiencies played a significant role in H&R Block/Tax Act,[27] where the merging parties presented evidence of cost savings in ten different areas (e.g., online information technology, a debit card, the corporate website, and software information technology). Applying the 2010 Merger Guidelines in evaluating the claimed efficiencies, the court questioned why the cost savings and certain IT efficiencies could not be obtained absent the merger. The court also found that the efficiencies were not verifiable because they were only based on the "experiential judgment" of managers in the business without specific facts or figures to support the claims.[28]

It is also worth noting that the court in *H&R Block* was skeptical of claimed efficiencies because of H&R Block's past integration failures. The court pointed to a smaller 2006 acquisition of another tax software company where H&R Block had estimated more conservative efficiencies over a three year horizon but failed to achieve them. Instead of crediting the company with having learned from those shortcomings, the court found that "this history only underscores the need for any claimed efficiencies to be independently verifiable in order to constitute evidence that can rebut the government's presumption of anticompetitive effects."[29] Thus, courts seem to accept the agencies' position that "[t]he best way to substantiate an efficiency claim is to demonstrate that similar efficiencies were achieved in the recent past from similar actions."[30]

Similarly, AT&T's abandoned acquisition of T-Mobile illustrates the uphill battle to demonstrate merger-specific and verifiable efficiencies with the agencies. Public papers filed in connection with the transaction highlighted that the parties did significant work and provided the agencies with detailed information and studies regarding the network enhancing efficiencies the parties believed would be achieved with the merger. The parties presented a set of complimentary models: one showing cost savings from network integrations and another showing an economic analysis of the resulting consumer welfare benefit.[31] But, in seeking injunctive relief, the DOJ stated that while it "gave serious consideration to the efficiencies that the merging parties claim would result from the transaction," the merging parties "had not demonstrated that the proposed transaction promised any efficiencies that would be sufficient to outweigh the transaction's substantial adverse impact on competition and consumers."[32] Further, the DOJ took the position that "AT&T could obtain substantially the same network enhancements that it claims will come from the trans-

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[26] Similarly, in *Swedish Match*, the court found that the claimed efficiencies of lowered fixed costs from consolidating operations and better capacity management, and lowered variable costs from more automation, were insufficient to rebut the increased concentration—and likely competitive harm—that would result from combining the largest producer of loose leaf tobacco manufacturer in the United States with the third largest producer. FTC v. Swedish Match, 131 F. Supp. 2d 151, 171–72 (D.D.C. 2000).

[27] United States v. H&R Block, Inc., 833 F. Supp. 2d 36 (D.D.C. 2011).

[28] *Id.* at 91.

[29] *Id.* at 91–92.

[30] U.S. Dep't of Justice & Federal Trade Comm'n, Commentary on the Horizontal Merger Guidelines 53 (2006) [hereinafter 2006 Commentary], *available at* http://www.justice.gov/atr/public/guidelines/215247.pdf.

[31] Fed. Commc'ns Comm'n, Staff Analysis & Findings ¶ 123 et seq., In re Applications of AT&T, Inc. & Deutsche Telekom AG, WT Docket No. 11-65 (Nov. 29, 2011), *available at* http://hraunfoss.fcc.gov/edocs_public/attachmatch/DA-11-1955A2.pdf.

[32] Press Release, U.S. Dep't of Justice, Justice Department Files Antitrust Lawsuit to Block AT&T's Acquisition of T-Mobile (Aug. 31, 2011), *available at* http://www.justice.gov/atr/public/press_releases/2011/274615.htm.

action if it simply invested in its own network without eliminating a close competitor."[33] This case illustrates that it can be particularly difficult for innovation efficiencies to prevail because, despite the agencies' recognition that mergers can result in more effective research and development or "may spur innovation," true innovation is difficult to quantify and verify, and, therefore, the agencies may remain skeptical of such claims.

Recent litigation against the FTC is not any more promising concerning the burden of establishing efficiencies, especially in light of the *Whole Foods*[34] preliminary injunction standard. In *FTC v. OSF Healthcare*, the court was "mindful of its limited role in [the injunction] proceedings and express[ed] no opinion on the ultimate merits of the proposed merger."[35] Despite the parties' identification of specific areas of cost savings from the consolidation, the court considered the potential for such efficiencies "that made business sense" as no guarantee of actual implementation and relied on conflicting expert testimony, ultimately finding no "confidence" that the efficiencies rebutted the strong structural presumption of anticompetitive effect.[36] The court granted the injunction allowing the matter to be further considered in the FTC administrative proceedings.

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While these recent cases demonstrate efficiencies arguments still play a role in merger analysis, they strongly suggest that any calculations or models must survive close and rigorous testing before being accepted.

Efficiencies Still Matter

Given this backdrop, it would be difficult to claim that efficiencies alone can save an otherwise anticompetitive merger. But while no cases have been won based on efficiencies alone,[37] there are numerous examples where efficiencies tipped the scale in favor of clearing the merger. For instance, in *Long Island Jewish Medical Center*, the parties claimed significant efficiencies across fifty different products and supported this claim with expert testimony.[38] The court found that while some of the claimed efficiencies were unlikely to be realized, the transaction in its totality would result in annual operating savings of approximately $25 to $30 million.[39] Even in *Arch Coal*, although $100 million of between $130 and $140 million in purported savings were found by the

33 Press Release, Justice Dep't Files Antitrust Lawsuit to Block AT&T's Acquisition of T-Mobile (Aug. 31, 2011), *available at* http://www.justice.gov/atr/public/press_releases/2011/274615.htm. The transaction was also subject to FCC approval. The FCC staff report suggested that FCC staff also conducted a number of sensitivity tests to the models and found the results varied too much based on the assumptions which themselves were subject to debate. As such, the staff could not credit the efficiencies claimed.

34 FTC v. Whole Foods Mkts., Inc., 548 F.3d 1028 (D.C. Cir. 2008). Under the holding in Whole Foods, it appears that the parties' efficiencies arguments may not receive much consideration because a district court need only "balance the likelihood of the FTC's success against the equities, under a sliding scale" and in its analysis a "district court should bear in mind the FTC will be entitled to a presumption against the merger on the merits . . . and therefore does not need detailed evidence of anticompetitive effect at this preliminary phase." *Id.* Accordingly, the FTC need not make any showing of irreparable harm, and "'private equities' alone cannot override the FTC's showing of likelihood of success." *Id.* at 1035. *Whole Foods* also made clear that at this preliminary stage the FTC does not "necessarily need to settle on a market definition" and can put forth alternate theories of anticompetitive harm without committing to one because "it just has to raise substantial doubts about a transaction." *Id.* at 1036.

35 FTC v. OSF Healthcare Sys. 852 F. Supp. 2d 1069, 1089 (N.D. Ill. 2012).

36 *Id.* at 1087–93.

37 *See, e.g.*, Robert Pitofsky, *Efficiency Consideration and Merger Enforcement: Comparison of U.S. and EU Approaches*, 30 FORDHAM INT'L L.J., 1413, 1418 (2006) ("There is no recorded instance in the United States where an otherwise illegal merger was found by a court not to violate the antitrust laws because of the presence of efficiencies.").

38 United States v. Long Island Jewish Med. Ctr., 983 F. Supp. 121, 147 (E.D.N.Y. 1997).

39 *Id.* at 148–49.

court to be questionable or overstated, the efficiencies in general were found "relevant to an assessment of the post-merger market and the potential benefits to consumers from cost reductions and increased competition," and supported the conclusion that there would not be a substantial lessening of competition.[40]

Similarly, in *FTC v. Butterworth Health Corp.*,[41] the district court recognized the importance of efficiencies, but only after considering detailed estimates of the capital investment savings and other operating efficiencies. While the FTC's expert criticized the degree of the projected savings, the court sided with the hospitals because they had done their homework. The court pointed out a "striking disparity in quality" between the experts:

> Defendants' experts were part of multi-disciplinary teams who spent as much as four months in Grand Rapids inspecting the hospital facilities and conducting hundreds of interviews. The FTC's expert admitted he had not been to Grand Rapids in over 20 years. He did not conduct independent capital avoidance and efficiencies studies, but merely critiqued those done by defendants' experts.[42]

The 2006 Commentary on the 1992/1997 Merger Guidelines[43] specifically identified a number of matters where the efficiencies arguments were central to the agencies' decision not to challenge the merger:

- In Toppan/DuPont, the DOJ analyzed a three-to-two merger in the market for high technology photomasks from which integrated circuits were made. It applied an auction model that predicted only small potential price increases. The DOJ concluded no net harm to competition would result from the transaction, taking into account a conservative estimate of the efficiencies.
- In Genzyme/Ilex, the FTC approved the transaction in large part because of "out-of-market" efficiencies. Although, the FTC found the transaction would reduce direct competition between the two firms, the merger promised substantial efficiencies in another use for the drugs. Instead of rejecting the merger in its entirety, the FTC cleared the deal with a remedy tailored to alleviate competitive concerns while still preserving the potential to achieve the efficiencies.
- Similarly, in Genzyme/Novazyme, the FTC cleared what it claimed to be a merger to monopoly in part because the combined firm would be able to develop a potential treatment for a rare disease faster than the companies could independently. But, it is important to note that the agencies typically view more skeptically combinations where innovation is central to competition between the merging firms.[44]
- In 2005, two separate telecommunications transactions, Verizon/MCI and SBC/AT&T, were approved in significant part because of the efficiencies. Central to the DOJ's decision not to challenge the mergers was its conclusion that the combinations provided the ability to sell

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40 *Arch Coal*, 329 F. Supp. 2d at 153.

41 FTC v. Butterworth Health Corp., 946 F. Supp. 1285 (W.D. Mich. 1996), *aff'd*, 121 F.3d 708 (6th Cir. 1997).

42 *Id.* at 1301.

43 2006 Commentary, *supra* note 30.

44 Richard G. Parker, Prepared Remarks before the Annual Briefing for Corporate Counsel (Sept. 16, 1998) ("That argument is not likely to succeed where innovation is a driving force behind competition. . . . We recognize that the reduction of R&D expenses may sometimes be a cognizable efficiency, but it is not when the result may be reduced competition."), *available at* http://www.ftc.gov/speeches/other/parker.shtm.

services across regions at lower costs by combining complimentary inputs.[45]

Moreover, it is not uncommon for the agencies to highlight efficiencies in their closing statements when clearing transactions. For example, in the DOJ's closing statement in the merger of Delta Air Lines and Northwest Airlines, efficiencies appeared to be one of the main reasons for allowing the transaction to proceed. The letter noted that "the merger will result in efficiencies such as cost savings in airport operations, information technology, supply chain economics, and fleet optimization that will benefit consumers."[46]

Parties must recognize that what they consider to be efficiencies from a business perspective may be very different from the kinds of efficiencies that will count for purposes of the antitrust analysis.

While one might be able to glean the impact of efficiencies from a closing statement, the confidential nature of agency review makes it difficult to understand precisely how the parties positioned an efficiencies defense and how it might have influenced the outcome. As a result, it is entirely possible that efficiencies play an even greater role in the close cases than can be detected.

Maximizing Credit for Efficiencies

In developing an efficiencies argument, parties must recognize that what they consider to be efficiencies from a business perspective may be very different from the kinds of efficiencies that will count for purposes of the antitrust analysis. Before signing a deal, parties often conduct significant quantitative analyses and hire consultants and bankers to assist in valuing the transaction and projecting the prospects for the combined firm. Many of these analyses include predicted efficiencies, including significant cost savings, benefits from more productive assets, access to more efficient or broader distribution networks, and the potential for collaboration on new products. But many of these business efficiencies might not be counted in an antitrust analysis because they are not merger specific or verifiable.

Typically, during the commercial negotiations phase of a deal, such issues are not of primary concern, and gun-jumping concerns—i.e., the prohibition of sharing competitively sensitive information before close—may add other practical difficulties to the parties' obtaining the level of detail necessary to make efficiencies estimates substantiated at the level the agencies would want. Nevertheless, starting to develop these arguments at an early stage is critical for efficiencies to be given any weight—and guidelines for clean teams, or independent third-party expert teams (which are inherently clean) can be established to resolve gun-jumping concerns related to more detailed information necessary to develop support for the efficiencies claims.

Therefore, in preparing to make the most persuasive efficiencies argument possible, the parties should consider the following:

- **Acknowledge the bar is set high for efficiencies evidence.** The parties bear the burden of presenting a well-supported and verifiable quantification of efficiencies. The agencies and the courts are going to put significant effort into reviewing the information submitted, including testing the assumptions and models the parties are using. Any doubts about quantification or ability to achieve the efficiencies are not likely to be resolved in favor of the merging parties.
- **Start early and be consistent.** Developing the strengths of an efficiencies argument *early* lets the parties use efficiencies affirmatively, not just defensively to counter a structural case against the merging parties. One of the lessons learned from *Staples* is that being consis-

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45 *See, e.g.*, Press Release, U.S. Dep't of Justice, Statement of the Department of Justice's Antitrust Division on Its Decision to Close Its Investigation of the Merger of Delta Airlines Inc. and Northwest Airlines Corp. (Oct. 29, 2008), *available at* http://www.justice.gov/atr/public/press_releases/2008/238849.pdf.

46 *See* 2010 Merger Guidelines, *supra* note 1, § 10.

tent from the beginning will make the existence of efficiencies appear less like a post-hoc rationalization. Identifying the limits of what can be substantiated from ordinary course-of-business documents and models is key to developing a strategy for presenting efficiencies arguments. For those transactions where the efficiencies are important to the deal rationale, the parties should take the time early in the process to substantiate the estimates. While clearing a deal based on efficiencies is an uphill battle given the high standards, efficiencies remain an important piece of the puzzle and may turn the tide in merger review. Thus, presenting a coherent and readily supported efficiencies argument at the outset is critical to the success of an efficiencies argument.

- **Explain in detail why the efficiencies are "merger specific."** As previous cases have demonstrated, antitrust analysis will not credit all efficiencies identified by the business. Only merger-specific efficiencies—those that could not practically be achieved without the merger—will be credited in the antitrust analysis. For example, cost savings that could be obtained independent of the merger by investment in more efficient production technology would be considered benefits that could be obtained via a "less restrictive alternative," i.e., without the merger, which raises no risk of the potential anticompetitive harm concerning the agencies. There are no rigid bounds for what alternatives are practically available, but arguments that a non-merger strategy to obtain similar benefits is not viable merely because it would cost more and take longer are not likely to be persuasive. The agencies and courts have tended to resolve any uncertainty against crediting the efficiencies. The agencies have found that certain efficiencies, such as those related to procurement, management, or capital cost, may be less likely to be merger specific or substantial.[46] Thus, when making efficiencies arguments, the parties should take great care to explain why the efficiencies would not be achievable absent the transaction, highlighting impossibilities more than mere inconveniences associated with the potential alternatives where possible.

Developing the strengths of an efficiencies argument early lets the parties use efficiencies affirmatively, not just defensively to counter a structural case against the merging parties.

- **Do not overlook low-hanging fruit.** The agencies have found that certain types of efficiencies, such as shifting production between facilities to reduce the merged firms' incremental costs, are more likely to be verifiable and substantial than others. Parties, therefore, should be sure to highlight these types of efficiencies where they can.
- **Use experts as appropriate.** As seen in *H&R Block*, *Oracle*, and *Staples*, courts are reluctant to rely on efficiencies analysis by subject matter experts within the company. The efficiencies in *Oracle* were predicated on the best projections of a senior executive, but were rejected because the court still found them to be mere speculation. At the same time, the 2010 Merger Guidelines state that "projections of efficiencies may be viewed with skepticism . . . when generated outside of the usual business planning process." Thus, experts must be used appropriately and, to the extent possible, incorporate materials and data the parties rely on in the ordinary course of business as the basis for their analysis. Experts developing and presenting efficiencies-related models should anticipate that any input assumptions of their models that are not based on such ordinary course information will be subjected to rigorous testing.

By taking into account these practical considerations, parties with significant efficiencies enhancing transactions can work to develop and present their efficiencies arguments in a way that maximizes the potential credit with the agencies. While efficiencies are not likely to compensate for severe structural concerns, in closer cases they can be a very effective tool to establish a positive frame of reference for the agency staff's review of the transaction. Proving efficiencies remains a challenging endeavor, but it remains clear that efficiencies can still be a persuasive factor in merger review analysis. ●