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appeal, filed an amended complaint which completely eliminated the charge that the agreement complained of affected the price of sugar in interstate commerce. . . . Despite the deletion from the complaint of the allegation concerning the price of sugar, the Court assumes, without allegation or evidence, that the price of sugar is affected and on that basis builds its thesis that the Sherman Act has been violated. . . . I would affirm the judgment of the District Court.

NOTES AND QUESTIONS ON *MANDEVILLE*

1. Should buyer cartels be illegal only when harm to downstream consumer welfare is proven? Much of the opinion focuses on whether the interstate commerce requirement of the statute has been met, an issue that has largely receded into unimportance as subsequent Supreme Court decisions made that requirement trivial to prove. *See* Chapter 1. But the issue of continuing relevance is that here the adverse intrastate effects were only on the sugar beet producers who sold in the local market, and consumers could not be harmed unless there were some adverse effect on the national (interstate) market for buying sugar. Should the statute be interpreted to require some adverse effect on consumers?

Given that the antitrust laws adopt a consumer welfare standard, it might seem that proof of harm to consumers should be required. But the antitrust laws do not require such proof. A simple justification is that: (a) to the extent the buyer cartel has any effect at all on the downstream market, it would be harmful to consumers; and (b) if the buyer cartel has no effect on the downstream market, it harms upstream producers with no benefit to consumers.

Suppose the local buying cartel had simply set a subcompetitive low price for sugar beets. This would result in lower local output of sugar beets, which would consequently lower the downstream sugar output of the California sugar beet refiners. If California sugar beet refiners produce a significant share of the nation's sugar or if other national sugar refiners could not easily and immediately expand production at the same cost to offset any reduction in California sugar output, a lowering of California sugar output would lower national sugar output and thus raise downstream sugar prices. This means that downstream consumers would be hurt by the upstream buying cartel. If instead California sugar beet refiners produce an insignificant share of the nation's sugar and other national sugar refiners could easily and immediately expand production at the same cost to offset any reduction in California sugar output, than a change in the sugar output of California sugar beet refiners would not alter national sugar prices. But even in this case, the California sugar beet refiners would still have incentives to fix subcompetitive low prices for sugar beets because that would increase their profit margin per beet.

Thus, to the extent buying cartel had any effect on downstream consumers, it would be negative. Requiring proof of harm to consumers would thus increase underdeterrence and harm to consumers (because errors will be made assessing that proof and the costs of such prove will result in fewer challenges) without any gain to consumers. Further, even in the best case scenario of no effect on consumers, the buyer cartel still harms upstream producers. It makes sense to protect producers from anticompetitive conduct when doing so causes no harm to consumer welfare. To be sure, the U.S. courts stress that antitrust law protects "competition, not competitors," but what this means is that antitrust law does not protect competitors at the *expense* of consumer welfare, which would clearly conflict with the consumer welfare standard. But antitrust law does protect producers from anticompetitive conduct that has no benefit to consumers.

2. ***Does the fact that beets prices were fixed based on downstream profits require inquiring into cartel's effect on downstream prices?*** The above analysis assumed a buying cartel that simply set a subcompetitive low price for sugar beets. However, here the challenged buyer agreement fixed California sugar beet prices based on a share of the refiner's sugar profits, which in turn depended on national sugar prices. Does that mean, as Justices Jackson and Frankfurter argued, that the plaintiffs should have had to prove that the restraint had an effect on national sugar prices? To consider the issue, suppose that sugar beet producers were initially getting competitive prices that gave them 50% of national sugar profits. Suppose further that the California sugar beet refiners agreed that from now on, the price to sugar beet producers would be set at only 1% of national sugar profits. Even if that restraint did not alter national sugar prices, it would clearly lower the upstream price for California sugar beets and thus lower local California sugar beet output, with all the possible effects noted above for a cartel that simply set a subcompetitive price for California sugar beets.

3. ***Does the fact that beets were fixed based on average profits eliminate any adverse effect?*** Are the above conclusions altered by the fact that here the buying cartel apparently did not lower the share of sugar profits given to sugar beet producers, but rather fixed sugar beet prices based on an *average* of the sugar profits of all three local sugar beet refiners? Although that feature means the agreement did not lower the average price paid for sugar beets in California, any effects it did have are still likely to be anticompetitive for the following reasons. By basing prices on average refiner profits, the agreement necessarily made the sugar beet purchase price lower for the most profitable refiner and higher for the other two refiners. Because all the refiners were selling sugar in a national market, presumably the sugar prices they received were the same, and thus the most profitable refiner must have had lower costs and been more efficient. Lowering the price paid by the most efficient refiner and raising the price paid by the less efficient refiners would at the margin decrease the sugar beet output sold to the more efficient refiner and increase the sugar beet output sold to the less efficient refiners. The effect of this shifting of output from the most efficient to the less efficient refiner would increase average California sugar refiner costs, which, to the extent it had any downstream effect, would likely increase sugar prices.

One might wonder why the California sugar refiners would want to enter into an agreement that would raise the prices two of them paid and

One implication of this ultimate test is that, even if the two elements were met, the failing firm defense would not apply if, without the merger, the firm would be liquidated in a way resulted in its assets being sold piecemeal to firms *within* the market. The justification for this conclusion is that such a liquidation would likely be less anticompetitive than having those assets all transferred to a merged firm that would gain anticompetitive market power. On the other hand, forcing liquidation in such a case might require inefficiently sacrificing the going-concern value of the firm. Why deny the failing firm defense in such cases? Probably the best explanation is that the failing firm defense is absolute, so recognizing it would immunize the merger even if the anticompetitive effects outweigh any efficiencies from preserving going concern value. Given its absolute nature, agencies and courts and agencies sensibly prefer to narrow the failing firm defense to cases where meeting the defense really disproves any possibility of anticompetitive effect, which is only in the extreme case when the assets would otherwise leave the market entirely. Denying the failing firm defense still allows agencies and courts to directly consider failing firm issues as bearing on the extent of anticompetitive effects and efficiencies under a general balancing rule-of-reason approach.

How can one decide what constitutes a good faith effort to obtain a reasonable alternative offer? Good faith cannot just mean selling to the highest bidder, because the buyer who would reap the greatest anticompetitive profits is likely be the highest bidder. But if a firm cannot just sell to the highest bidder, how much below that bid still constitutes a reasonable alternative offer? Reflecting the ultimate test, footnote [illegible] of the guidelines indicates that an alternative offer is reasonable if it exceeds the value of the assets *outside* the market and would create less anticompetitive effect than the merger.

6. THE RELEVANCE OF BUYER POWER OR VIEWS

a. MERGERS BETWEEN BUYERS THAT CREATE BUYER POWER

It has long been understood that: "The exercise of market power by buyers, or monopsony, can impose social costs equivalent to those imposed by monopoly."[46] This point was strongly reaffirmed in the *Weyerhaeuser* case excerpted for Chapter 3. It is no defense that the creation of monopsony power lowers prices in the purchasing market. Those lower prices are *sub*competitive prices and thus (like *supra*competitive prices) produce a lower and subcompetitive market output. This will be true even if sellers have no fixed costs as long as they have increasing marginal costs.[47] A buyer with market power will maximize profits by paying only a subcompetitive price even though that lowers output because it will take into account the fact that any

[46] IV AREEDA, HOVENKAMP & SOLOW, ANTITRUST LAW ¶ 980 (rev. ed. 1998); *see generally* BLAIR & HARRISON, MONOPSONY (1993).

[47] *See, e.g.,* HOVENKAMP, FEDERAL ANTITRUST POLICY § 1.2b (1994).

additional marginal purchases it can make by increasing the price will increase the market price it pays for all inframarginal purchases.[48]

The adverse effects of buyer market power may seem counter-intuitive because the consequence is lower prices in the purchasing market. But these lower prices are *sub*competitive prices and thus (like *supra*competitive prices) produce a lower and subcompetitive market output and quality. Thus, the intuition proves false for at least three reasons.

(1) Where the firm with buyer market power also has selling market power in a downstream market, the predictable result of upstream monopsony power is lower downstream output, and thus *higher* (supracompetitive) prices in the downstream market in which the powerful buyer sells.[49]

(2) Even without higher prices in a downstream market, the creation of monopsony power remains anticompetitive in the upstream market and harmful to sellers in it.[50]

(3) Even if an upstream exercise of buyer market power did turn out to lower downstream consumer prices, those lower prices would remain *sub*competitive prices that create *sub*competitive levels of market output and quality downstream. These subcompetitive levels of output and quality would remain harmful to consumers, who by definition would have been willing to pay more for the output and quality level that a competitive market would have afforded them.

Further, if price discrimination is possible, then a buyer with market power that wants to gain a competitive advantage downstream may be able to insist on a large discount compared to what the sellers charge

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[48] For a seller with market power, its marginal revenue is lower than the price it charges to make the marginal sale because it has to take into account that any price cut lowers the prices it makes on the inframarginal sales. Thus, the seller with market power does not produce the output where price equals its marginal costs but rather the lower output where its marginal revenue equals its marginal costs. Likewise, for a buyer with market power, its marginal outlay is higher than the price it pays to make the marginal purchase because it has to take into account that any price increase raises the prices it pays on inframarginal purchases. Thus, the buyer with market power does not offer prices high enough to result in an output where price equals its marginal demand, but rather demands subcompetitive prices that produce a lower output where its marginal outlay equals its marginal demand.

[49] *Id.*; Roger D. Blair & Jeffery L. Harrison, *Antitrust Policy and Monopsony*, 76 CORNELL L. REV. 297, 335 (1991) ("Substantive economic analysis reveals that it is an error to infer that the lower prices a monopsonist obtains translate into lower ultimate prices for the monopsonists' customers.").

[50] *See* Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber, 549 U.S. 312 (2007) (articulating test for predatory overbuying that imposes liability for enhancing upstream monopsony power in a local market rather than requiring anticompetitive effects in the downstream national market); Mandeville Island Farms v. American Crystal Sugar, 334 U.S. 219 (1948) (condemning a buying cartel in a regional sugar beet market without any proof that it would have a price effect on the downstream national market in refined sugar); United States v. Pennzoil, 252 F.Supp. 962 (W.D.Pa. 1965) (condemning merger that created local monopsony power in Pennsylvania crude oil market even though it seemed unlikely to affect output in downstream worldwide market for refined oil); United States v. Rice Growers Ass'n, 1986–2 Trade Cas. (CCH) ¶ 67,288 (E.D. Cal.) (condemning merger that created local monopsony power in California paddy rice market even though it seemed unlikely to affect output in downstream worldwide market for milled rice).

other buyers who compete with the powerful buyer downstream. This may distort downstream competition. Further, the upstream result can be that the powerful buyer pays a *sub*competitive price on its purchases whereas rival buyers pay a *supra*competitive price for their purchases. Both *sub*competitive and *supra*competitive prices lead to lower output than the competitive price. The *sub*competitive prices will lower output by making sellers less willing to produce for the powerful buyer; the *supra*competitive prices will lower output by making rival buyers less willing to purchase.

U.S. DOJ/FTC, Horizontal Merger Guidelines

(2010).

12. Mergers of Competing Buyers

Mergers of competing buyers can enhance market power on the buying side of the market, just as mergers of competing sellers can enhance market power on the selling side of the market. Buyer market power is sometimes called "monopsony power."

To evaluate whether a merger is likely to enhance market power on the buying side of the market, the Agencies employ essentially the framework described above for evaluating whether a merger is likely to enhance market power on the selling side of the market. In defining relevant markets, the Agencies focus on the alternatives available to sellers in the face of a decrease in the price paid by a hypothetical monopsonist.

Market power on the buying side of the market is not a significant concern if suppliers have numerous attractive outlets for their goods or services. However, when that is not the case, the Agencies may conclude that the merger of competing buyers is likely to lessen competition in a manner harmful to sellers.

The Agencies distinguish between effects on sellers arising from a lessening of competition and effects arising in other ways. A merger that does not enhance market power on the buying side of the market can nevertheless lead to a reduction in prices paid by the merged firm, for example, by reducing transactions costs or allowing the merged firm to take advantage of volume-based discounts. Reduction in prices paid by the merging firms not arising from the enhancement of market power can be significant in the evaluation of efficiencies from a merger, as discussed in Section 10.

The Agencies do not view a short-run reduction in the quantity purchased as the only, or best, indicator of whether a merger enhances buyer market power. Nor do the Agencies evaluate the competitive effects of mergers between competing buyers strictly, or even primarily, on the basis of effects in the downstream markets in which the merging firms sell.

> *Example 24:* Merging Firms A and B are the only two buyers in the relevant geographic market for an agricultural product. Their merger will enhance buyer power and depress the price paid to farmers for this product, causing a transfer of wealth from farmers to the merged firm and inefficiently reducing supply. These effects can arise even if the merger will not lead to any increase in the price charged by the merged firm for its output. . . .

b. SHOULD MERGERS BETWEEN SELLERS BE DEEMED CONSTRAINED BY BUYER POWER?

U.S. DOJ/FTC, Horizontal Merger Guidelines

(2010).

8. Powerful Buyers

Powerful buyers are often able to negotiate favorable terms with their suppliers. Such terms may reflect the lower costs of serving these buyers, but they also can reflect price discrimination in their favor.

The Agencies consider the possibility that powerful buyers may constrain the ability of the merging parties to raise prices. This can occur, for example, if powerful buyers have the ability and incentive to vertically integrate upstream or sponsor entry, or if the conduct or presence of large buyers undermines coordinated effects. However, the Agencies do not presume that the presence of powerful buyers alone forestalls adverse competitive effects flowing from the merger. Even buyers that can negotiate favorable terms may be harmed by an increase in market power. The Agencies examine the choices available to powerful buyers and how those choices likely would change due to the merger. Normally, a merger that eliminates a supplier whose presence contributed significantly to a buyer's negotiating leverage will harm that buyer.

> *Example 22:* Customer C has been able to negotiate lower pre-merger prices than other customers by threatening to shift its large volume of purchases from one merging firm to the other. No other suppliers are as well placed to meet Customer C's needs for volume and reliability. The merger is likely to harm Customer C. In this situation, the Agencies could identify a price discrimination market consisting of Customer C and similarly placed customers. The merger threatens to end previous price discrimination in their favor.

Furthermore, even if some powerful buyers could protect themselves, the Agencies also consider whether market power can be exercised against other buyers.