THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

UNITED STATES OF AMERICA, Plaintiff, v. ABITIBI-CONSOLIDATED INC. and BOWATER INC., Defendants.	CASE NO: 1:07-cv-1912 (RMC) JUDGE: Collyer, Rosemary M. DECK TYPE: Antitrust DATE STAMP: August 8, 2008

REPLY BY THE UNITED STATES TO NAA'S OPPOSITION TO MOTION FOR ENTRY OF THE PROPOSED FINAL JUDGMENT

INTRODUCTION

The United States and the Newspaper Association of America ("NAA") agree that the issue before the Court is whether the relief that the United States has secured in the proposed Final Judgment meets the Tunney Act's public interest standard.[1] Under this standard,

> balancing of competing social and political interests affected by a proposed antitrust consent decree must be left, in the first instance, to the discretion of the Attorney General. The court's role in protecting the public interest is one of insuring that the government has not breached its duty to the public in consenting to the decree.

United States v. Bechtel Corp., 648 F.2d 660, 666 (9th Cir. 1981). As the United States explains below, the public interest standard is a reasonableness test that incorporates substantial deference to the Attorney General.

The United States disagrees with NAA on whether the relief required by the proposed

[1]Antitrust Procedure and Penalties Act, 15 U.S.C. § 16 (b)-(h) (herein, the "Tunney Act" or "Act").

Final Judgment is adequate to the preserve competition that would have been lost as a result of the defendants' merger. The decision to require that relief, the divestiture of the Snowflake mill in Snowflake, Arizona, was the result of a comprehensive nine-month investigation and was based on the same detailed economic modeling that the United States used in deciding to challenge the parties' transaction by bringing this case in the first instance. NAA's claim that the Snowflake divestiture is inadequate is based on flawed economic arguments that AbitibiBowater, Inc. ("AbitibiBowater") exercised market power post-merger by closing capacity and increasing newsprint prices. The United States attaches herewith the Declaration of Dr. Nicholas Hill to explain how the United States crafted the proposed remedy and to demonstrate why NAA is wrong. In making a public interest determination, of course, the Court need not determine which economist is correct; it only needs to find that the United States has presented a reasonable basis for the proposed settlement.

This reply brief is organized as follows: after discussing the applicable law, the United States explains why the Snowflake divestiture is an appropriate remedy. The United States then explains why the nominal price increases upon which NAA relies do not demonstrate that AbitibiBowater has exercised market power and appear instead to be the result of non-merger related economic trends – a conclusion reinforced by the fact that newsprint price trends are consistent with price trends for similar high volume paper products not affected by the merger. In addition, the United States explains that NAA ignores a critical fact: the mills that AbitibiBowater closed were losing money during the investigation and at the time that they were closed, which is enough in itself to undermine NAA's economic conclusions. Finally, the United States explains that the evidentiary hearing requested by NAA is unprecedented and unnecessary.

ARGUMENT

I. The Court Must Enter The Proposed Final Judgment If It Determines That The Proposed Final Judgment Meets The Public Interest Standard.

The Tunney Act provides that before entering the parties' settlement as its judgment, the Court must "determine that the entry of such judgment is in the public interest." 15 U.S.C. § 16(e)(1). Although the Act provides a non-exclusive list of factors that the Court "shall consider" in making its determination,[2] the Act offers no explicit directives regarding the standard the Court is to apply in making its determination. Indeed, the statute does not define the key phrase "in the public interest." *United States v. SBC Communications, Inc.*, 489 F. Supp. 2d 1, 10 (D.D.C. 2007) ("*SBC*"). In the three decades since its enactment, the courts (in particular, those of this circuit) have drawn on the Act's language, structure, context, and legislative history to flesh out that standard and the nature of this Court's task. As Judge Sullivan found in his recent decision

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[2] A court is to consider these factors (15 U.S.C. § 16(e)(1)):

> (A) the competitive impact of such judgment, including termination of alleged violations, provisions for enforcement and modification, duration of relief sought, anticipated effects of alternative remedies actually considered, whether its terms are ambiguous, and any other competitive considerations bearing upon the adequacy of such judgment that the court deems necessary to a determination of whether the consent judgment is in the public interest; and
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> (B) the impact of entry of such judgment upon competition in the relevant market or markets, upon the public generally and individuals alleging specific injury from the violations set forth in the complaint including consideration of the public benefit, if any, to be derived from a determination of the issues at trial.

Prior to a 2004 amendment to the Tunney Act, the section provided that the court "may," rather than "shall," consider the listed factors, and there were some differences in the factors listed. Overall, however, "the 2004 amendments effected minimal changes" to the statute. *United States v. SBC Communications, Inc.*, 489 F. Supp. 2d 1, 11 (D.D.C. 2007) ("*SBC*").

examining the effect of the 2004 amendments to the Act, the "body of law interpreting the Tunney Act's vague language" continues to govern post-amendment Tunney Act proceedings. *Id.* at 11.

The United States has alleged conduct violating the antitrust laws – the defendants' planned merger – and the competitive harm that would result if the merger were permitted to go forward as defendants contemplated. The United States' settlement expresses its conclusion that the proposed decree adequately remedies (or prevents) the harm alleged in the Complaint, and that it would therefore be in the public interest for the Court to enter it.[3] The sole question for the Court is whether to reject that conclusion.

A court does not properly reject a proposed consent decree on the ground that a better decree can be imagined. The test instead is whether "the remedies [are] so inconsonant with the allegations charged as to fall outside of the 'reaches of the public interest.'" *Microsoft*, 56 F.3d at 1461; *see SBC*, 489 F. Supp. 2d at 16 (noting that there "is no indication . . . that Congress intended to overrule [*Microsoft*'s 'reaches of the public interest'] holding" by the 2004 Amendments). Thus a court may not "engage in an unrestricted evaluation of what relief would best serve the public interest." *United States v. BNS, Inc.*, 858 F.2d 456, 462 (9th Cir. 1988) (citation omitted). Instead, it must recognize that Congress intended that the applicable public interest concept encompass "compromises made for non-substantive reasons inherent in the

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[3]The Court's task here is not to determine the appropriate remedy for a violation of the antitrust laws, as if the case had been litigated and defendants found liable. A settlement is before the Court, and "there are no *findings* that the defendant has actually engaged in illegal practices." *United States v. Microsoft Corp.*, 56 F.3d 1448, 1460-61 (D.C. Cir. 1995). Thus, "for the district judge to assume that the allegations in the complaint have been formally made out is unwarranted." *Id.* at 1461. Moreover, no trial record exists, because the case settled before trial. For a Tunney Act court to create such a record to inform its determination would effectively require trial-type proceedings, depriving the parties of the benefit of resolving cases by settlement rather than litigation.

process of settling cases through the consent decree procedure," H.R. Rep. No. 93-1463, at 12 (1974), *reprinted in* 1974 U.S.C.C.A.N. 6535, 6542. Embodied in precedent, the broad "reaches of the public interest" standard logically follows from the Tunney Act's basic concept of judicial consideration of a *settlement*,[4] and rejects the view that a court may simply "interpose its own views of the appropriate remedy over those the government seeks as part of its overall settlement." *Id.* at 1458.

After a court addresses the specific factors listed in the Tunney Act, its public interest determination properly focuses on whether the terms of the decree are ambiguous, whether the court "can foresee difficulties in implementation," and whether the proposed decree, as opposed to defendants' conduct or other causes, would "positively injure[]" third parties. *Microsoft*, 56 F.3d at 1462.[5] But the primary focus in almost every case is whether "the remedies provided in the decree [are] adequate to the allegations in the complaint," *id.* at 1457, in light of the "reaches of the public interest" standard.

In these circumstances, where an expert executive branch agency conducts an extensive investigation and concludes that the public interest is served by a particular settlement, a court should exercise considerable caution before declining to enter the proposed judgment. The

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[4]If courts acting under the Tunney Act disapproved proposed consent decrees merely because they did not contain the exact relief which the court would have imposed after a finding of liability, defendants would have no incentive to consent to judgment and this element of compromise would be destroyed. The consent decree would thus as a practical matter be eliminated as an antitrust enforcement tool, despite Congress' directive that it be preserved. *United States v. American Tel. & Tel. Co.*, 552 F. Supp. 131 (D.D.C. 1982), *aff'd sub nom. Maryland v. United States*, 460 U.S. 1001 (1983). *See also Microsoft*, 56 F.3d at 1456 ("The Tunney Act was not intended to create a disincentive to the use of the consent decree.").

[5]No one has alleged that any of these matters raise concerns about the proposed decree in this proceeding.

decision to settle properly lies within the agency's "rather broad discretion." *Microsoft*, 56 F.3d at 1461. The "balancing of competing social and political interests affected by a proposed antitrust consent decree must be left . . . . to the discretion of the Attorney General." *Bechtel*, 648 F.2d at 666.

Beyond deference to the Attorney General's implicit balancing of interests, the court properly gives deference to the United States' judgments as to the efficacy of remedial provisions. While the degree of deference may vary with the extent of the court's familiarity with the market and other factors, *Microsoft*, 56 F.3d at 1461, the Court of Appeals has made clear that even a court with considerable relevant expertise should not lightly reject the United States' predictions. *Id.*[6]

Accordingly, the question is not whether the United States' view of the efficacy of the remedies provided in the proposed decree is correct, but rather whether the United States has established an "ample foundation for [its] judgment call" and thus shown "its conclusion reasonable." *Microsoft*, 56 F.3d at 1461; see also *SBC*, 489 F. Supp. 2d at 21 ("Even accounting for [shortcomings that could reduce the effectiveness of the proposed settlements], the United States has presented a reasonable basis for concluding that the proposed settlements will replace much of the competition lost to the mergers, if perhaps not all of it. Therefore, the Court finds that the proposed settlements are reasonably adequate, and thus within the reaches of the public interest.").

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[6]Thus, in the case of the AT&T decree – "a decree the oversight of which had been the business of a district judge for several years," *Microsoft*, 56 F.3d at 1460, the Court of Appeals instructed that the district judge should not reject an agreed-upon modification of the decree unless it had "'exceptional confidence that adverse antitrust consequences [would] result – perhaps akin to the confidence that would justify a court in overturning the predictive judgments of an administrative agency." *Id.* (quoting *United States v. Western Electric Co.*, 993 F.3d 1572, 1577 (D.C. Cir. 1993)).

II. The United States' Judgment Regarding the Scope of Relief Is Reasonable

The relief required under the proposed Final Judgment – the divestiture of the Snowflake, Arizona newsprint mill – remedies the harm to competition alleged in the Complaint and easily satisfies the public interest standard.[7] During the course of its comprehensive nine-month investigation, the United States conducted extensive discovery pursuant to 15 U.S.C. §§ 1311-1314, employed significant resources to review and analyze this information, determined that the proposed merger would result in a substantial lessening of competition in the North American newsprint market, and reached the conclusion that the divestiture of the Snowflake mill would restore the competition that the merger would have otherwise eliminated.[8] As part of this investigation, the United States obtained a substantial production of documents and information from the merging parties and issued 37 Civil Investigative Demands to third parties. In total, the

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[7] As explained in the United States' Competitive Impact Statement and Response to Public Comments, the United States' investigation found that under existing newsprint industry market conditions, such as sharply declining demand, the merged firm's loss of newsprint capacity from the divested Snowflake mill would reduce its total capacity such that it would not have enough newsprint capacity to benefit sufficiently from the post-merger price increase to offset the costs associated with shutting down profitable mills. (United States' Response to Public Comments, at 10-11 & 14-15; Competitive Impact Statement, at 7-8).

[8] NAA characterizes the United States' assertion that it has better data that it cannot divulge as the "trust us" defense and implies that the United States should disclose the confidential and competitively sensitive information upon which it bases its analysis. (NAA Memorandum, at 14). Such a practice could be harmful to antitrust enforcement and the United States is unaware of any Court that has required the United States to disclose antitrust investigatory information to an amicus. The United States was able to efficiently obtain information in this case in part because of the Antitrust Division's strict policy against disclosing – and strong record of protecting – confidential information. If Courts were to make a practice of requiring disclosure of such confidential information to trade associations and other third parties, companies may be more likely to resist discovery, making it more difficult for the United States to obtain the information it needs to make proper enforcement decisions. Courts could also place an additional burden upon themselves of overseeing motion practice relating to Civil Investigative Demands. *See* 15 U.S.C. § 1314(1).

United States received and considered more than 150,000 pages of material. The United States also conducted more than 60 interviews with customers, competitors, and other individuals with knowledge of the industry, including NAA.

To analyze the likely competitive effects of the merger, the United States used standard microeconomic theories to model competition in the newsprint industry – analyzing a comprehensive data set of prices, sales, production volumes, individual mill costs, capacities and forecasts of North American newsprint demand. (*See* Response to Public Comments, at 14-15. *See also* Competitive Impact Statement, at 7-9 ("CIS")). To help the Court understand the United States' analysis and why NAA's claims are not correct, the United States is submitting with this Reply the Declaration of Dr. Nicholas Hill, a Research Economist with the Department of Justice, which, *inter alia*, discusses the methodology the Department employed in reaching its conclusion.

This economic model used by the United States predicted that given mill costs and falling demand, Abitibi-Consolidated Inc. ("Abitibi") and Bowater Inc. ("Bowater") would close unprofitable capacity regardless of the merger. (Hill Declaration, ¶ ¶ 9-11). The model also predicted, however, that the merger would likely cause the combined firm to close profitable plants as well in order anticompetitively to increase the price of newsprint. (*Id*.) The merger created this incentive by combining the newsprint production capacity of the two firms, thereby increasing the volume of newsprint over which the combined firm would benefit from a price increase.

The United States used this same economic model to identify a divestiture that would be sufficient to remove the merged firm's incentive to close profitable capacity by reducing the volume of production over which the merged firm would benefit from a price increase. (*Id*. at 11). When an expert agency uses standard economic models to predict anticompetitive effects and then uses

these standard models to fashion relief, there is certainly a reasonable basis for determining that the settlement proposed by the United States is in the public interest.

III. Post-Merger Increases In Newsprint Prices Are More Consistent With Subsequent Non-Merger-Related Events Such As Input Cost Increases Than With Market Power

NAA claims that post-merger increases in nominal newsprint prices prove that the merged firm is exercising market power. However, NAA's assertion that the merger caused newsprint prices to increase is not persuasive when one looks at real newsprint prices, which account for inflation. Real newsprint prices are actually lower than the nominal prices that NAA reports and recent fluctuations in input prices, currency exchange rates, and other factors played important roles in the recent newsprint price increases that NAA has identified. Without further analysis of input costs, exchange rate fluctuations, and other factors that have also driven prices higher for a variety of other paper grades, the general observation by NAA's expert, Mr. John H. Preston, that newsprint prices have increased fails to support his conclusion that AbitibiBowater is exercising market power as a result of the merger. (*See* Hill Declaration, ¶¶ 12, 22-23).

1. Real Newsprint Prices Have Trended Downward Over Time and Actually Have Declined Since The Merger Announcement

Dr. Hill reviewed ten years of public newsprint sales data and adjusted the data for inflation. The real newsprint price data make it clear that the recent increase in newsprint prices is neither dramatic nor unprecedented, and that the nominal price increases NAA relies upon are not a result of an exercise of market power by the merged firm, but instead are entirely consistent with the volatile history of newsprint prices. (Hill Declaration, ¶ ¶ 12-15, 19). Real newsprint prices appear to be trending downward over time. (*Id.* at ¶ 19). In fact, the real price of newsprint is lower today than when the merger was announced. (*Id.* at ¶ 15). By ignoring the larger context,

focusing on a short time period, and presenting only a limited amount of information to the Court, NAA tells an incomplete and misleadingly simple story.

2. Currency Exchange Rates Have Affected U.S. Newsprint Prices as Canadian Producers Have Less Incentive To Produce Newsprint

NAA's expert, Mr. Preston, recognizes that a rising Canadian dollar relative to the American dollar raises the cost of Canadian production. (Preston Declaration, ¶ 53). However, Mr. Preston fails to adjust properly his analysis for currency changes over time and therefore does not account for a significant non-merger effect on prices in the newsprint industry. (*See* Hill Declaration, ¶ ¶ 16-19).

The exchange rate and its effect on Canadian producers are important to American newsprint consumers because more than half of the newsprint consumed in the United States is produced in Canada and many of the marginal newsprint producers, whose costs determine industry pricing, are located in Canada. (*Id.* at ¶ 16). In addition, Canadian producers have had less incentive to continue producing newsprint as their manufacturing costs have increased while their real revenues have not kept pace with these costs. (*Id.* at ¶ 17). One reason the cost of producing newsprint in Canada has increased is because the Canadian dollar has gained against the American dollar. (*Id.* at ¶ 16). Meanwhile, the average real price that Canadian producers receive for newsprint in Canadian dollars has fallen over time. (*Id*. at ¶ 17). These facts are also consistent with Dr. Hill's observation that it is Canadian – rather than American – mills which have reduced capacity as the Canadian dollar has gained value relative to the American dollar. (*Id*. at ¶ 27).

3. Input Costs Have Increased and Price Trends of Other Grades of Paper Are Similar to Newsprint

Dr. Hill posits that another way to determine whether AbitibiBowater has been exercising

market power or simply responding to rising input costs is to compare price trends for newsprint with products that have similar input costs. (Hill Declaration, ¶ 22). Since the merger was announced, the costs of fiber and fuel – two of newsprint's and similar paper products' major inputs – have increased significantly. (*Id.* at ¶ 14, n.6). Dr. Hill then demonstrates that the prices of three other grades of paper also rose significantly. (*Id.* at ¶ 23). The fact that the prices of newsprint and other grades of paper rose together suggests that factors other than the merger have driven newsprint prices higher, and undermines NAA's assertion that market power explains the nominal newsprint price increases that have been observed post-merger.

IV. NAA's Market Power Argument Ignores Important Facts

A. The Merged Firm Has Closed Only Unprofitable Mills

NAA adopts the Complaint's theory of harm that the combined firm would have the incentive to close profitable mills earlier than it would absent the merger. (NAA Memorandum, at 5). Relying on a dominant firm theory, NAA recognizes that a test for whether a firm is dominant is the firm's ability to close profitable mills:

> In a competitive market, the owner of a mill will continue to produce as the mill **covers its operating costs** and makes some contribution, however small, to fixed costs. Closing a mill that is still able to sell its output at a **profit** above its operating costs is a luxury that only a firm with market power can afford . . . .

(NAA Memorandum, at 9-10 (emphasis added)). NAA then goes on to assert that AbitibiBowater closed 610,000 metric tonnes of newsprint capacity in late 2007 "in an exercise of market power," which has caused newsprint prices to increase. (*Id.* at 11. *See also id.* at 7-10).

NAA's explanation of the exercise of market power by a dominant firm – in this instance AbitibiBowater – through closing profitable mills fatally disregards the fact that all the evidence

available indicates that the mills that AbitibiBowater closed were actually unprofitable. (Hill Declaration, ¶ 25 (quoting AbitibiBowater Executive Chairman John Weaver as stating: "All of the capacity closed was in a negative cash position.")). The United States has confirmed the unprofitability of the closed mills by reviewing the defendant's confidential profit and loss statements at these mills. The United States explained that "the three mills that AbitibiBowater closed after the merger were unprofitable" in its Response to Public Comments, (Response to Public Comments, at 9), a public document that was filed with this Court and which was served on NAA. Nevertheless, NAA has ignored this critical fact. It has failed to respond to the United States' assertion in this proceeding or to AbitibiBowater's similar statement to the financial community, and it has not provided any evidence that the closed mills were profitable.

NAA's faulty factual assumption that the mills that closed were profitable leaves it with no evidence that AbitibiBowater exercised market power as a dominant firm. The United States agrees that closing profitable mills may be some evidence that market power was exercised. Here, however, NAA's factual premise is simply not true.

B. Other Newsprint Producers Are Closing Mills

If AbitibiBowater were exercising market power in order to drive newsprint prices up, other firms in the industry would have a strong incentive to keep their mills open and even attempt to increase production in order to profit from those higher prices. (Hill Declaration, ¶ 26). However, several other firms also closed capacity in 2007 and 2008. (*Id.*). That these firms closed their mills is not consistent with NAA's claim that AbitibiBowater is a dominant firm exercising market power. (*Id.*). Instead, these closures suggest that the combined firm's decision to reduce unprofitable capacity was driven by factors other than the merger. (*Id.*).

V. Granting NAA's Request For An Evidentiary Hearing Would Be Unprecedented And Such A Hearing Is Unnecessary

Despite stating that the existing record is "more than adequate" to make a public interest determination, (NAA Memorandum, at 14), NAA contends that "if this matter is to be decided based on a choice between competing data sets and economic models," then an evidentiary hearing is needed. (*Id.*). That is not the legal standard, however. The Court is not faced with a choice between competing data sets and economic models, but with the question of whether the proposed Final Judgment is in the public interest. The record is more than adequate for the Court to decide the question that is actually before it, and thus an evidentiary hearing is both unnecessary and ill-advised.[9]

Although the Tunney Act permits a court to conduct an evidentiary hearing when necessary, 15 U.S.C. § 16(f), Congress contemplated that "the trial judge will adduce the necessary information through the least complicated and least time-consuming means possible." S. Rep. No. 93-298, at 6 (1973) ("Senate Report"); *accord* H.R. Rep. No. 93-1463, at 8 (1974), reprinted in 1974 U.S.C.C.A.N. 6535, 6539 ("House Report"). Ordinarily, this principle rules out an evidentiary hearing.[10] Indeed, the United States is unaware that an evidentiary hearing has

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[9]A Court that wishes to compare economic models and recreate the investigation would preside over a significant discovery process. The United States was able to conduct a comprehensive merger review because it dedicated a staff of up to ten attorneys and two economists, plus a support staff such as paralegals, research assistants, and clerical and technical staff. Updating the review and providing the Court with an updated set of facts to compare the competing economic models would require the entry of a protective order and an extensive period for significant discovery, including discovery outside of the United States.

[10]The various materials the Tunney Act does require, *see* 15 U.S.C. § 16(b), together with the record (if any) created prior to settlement, will usually suffice. *See United States v. Enova Corp.*, 107 F. Supp. 2d 10, 17 (D.D.C. 2000) ("Tunney Act expressly allows the court to make its public interest determination on the basis of the competitive impact statement and response to

ever been held in a Tunney Act proceeding in any jurisdiction.[11]

NAA's argument does not warrant departing from standard Tunney Act practice in this case. The Court must decide whether entry of the proposed decree would be within the "reaches of the public interest," which in turn requires deciding not whether the United States' conclusion expressed in the CIS and in Dr. Hill's Declaration is correct, but rather whether "the government has presented a reasonable basis for concluding that the proposed settlements will replace much of the competition lost to the merger[]." *SBC*, 489 F. Supp. 2d at 21. That question is easily answered here on the basis of the existing record and it is unnecessary to take the unprecedented step of holding an evidentiary hearing to determine whether entry of the proposed Final Judgment is in the public interest.

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comments alone"). *See also* The Antitrust Procedures & Penalties Act: Hearings on S. 782 & S. 1088 Before the Subcomm. on Antitrust & Monopoly of the Senate Committee on the Judiciary, 93d Cong., at 152-53 (1973) ("Senate Hearings") (testimony of Hon. J. Skelly Wright) ("an experienced judge, who does have the facility of getting to the point and getting others to get to the point, can arrive at a public interest determination in most cases without using" additional tools); Senate Report at 6 ("[w]here the public interest can be meaningfully evaluated simply on the basis of briefs and oral arguments, that is the approach that should be utilized"). The 2004 amendments to the Tunney Act explicitly stated that nothing in § 16(f) "shall be construed to require the court to conduct an evidentiary hearing." 15 U.S.C. § 16(f)(2). Even absent a settlement, no evidentiary hearing on relief is required where there are "no disputed factual issues regarding the matter of relief." *United States v. Microsoft Corp.*, 253 F.3d 34, 101 (D.C. Cir. 2001) (en banc) (per curia).

[11]The United States searched Antitrust Division records for the past twenty years and also conducted a Westlaw search for Tunney Act evidentiary hearings without finding any indication that such a hearing has ever been held.

CONCLUSION

For the reasons set forth in this Memorandum, the Motion To Enter the Proposed Final Judgment, the United States' Response to Public Comments, and the CIS, there is plainly a reasonable basis for the United States' conclusion that the proposed Final Judgment is in the public interest. The United States therefore requests that the Court so find, deny NAA's request for an evidentiary hearing, and enter the proposed Final Judgment.

Dated: August 8, 2008

Respectfully Submitted,

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CERTIFICATE OF SERVICE PURSUANT TO LOCAL RULE 5.4

I hereby certify that on August 8, 2008, I caused a copy of the foregoing Reply by the United States to NAA's Opposition to Motion for Entry of the Proposed Final Judgment to be served on the following individuals:

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