UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF KENTUCKY
SOUTHERN DIVISION at LONDON

UNITED STATES OF AMERICA, et al. Plaintiffs, v. DAIRY FARMERS OF AMERICA, INC., et al. Defendants.	)	Civil Action No.: 6:03-206-KSF

RESPONSE OF PLAINTIFF UNITED STATES TO
PUBLIC COMMENTS ON THE PROPOSED FINAL JUDGMENT

Pursuant to the requirements of the Antitrust Procedures and Penalties Act ("APPA" or "Tunney Act"), 15 U.S.C. § 16(b)-(h), the United States hereby files comments received from members of the public concerning the proposed Final Judgment in this civil antitrust suit and the responses by the United States to these comments. The United States and Commonwealth of Kentucky will move the Court for entry of the proposed Final Judgment after the public comments and this Response have been published in the *Federal Register*, pursuant to 15 U.S.C. § 16(d).

I. BACKGROUND

The United States and Commonwealth of Kentucky (the "government") filed a civil antitrust Complaint under Section 15 of the Clayton Act, 15 U.S.C. § 25, on April 24, 2003, alleging that the acquisition by Dairy Farmers of America, Inc. ("DFA") of its interest in

Southern Belle Dairy Co., LLC ("Southern Belle") violated Section 7 of the Clayton Act, 15 U.S.C. § 18. An Amended Complaint was filed on May 6, 2004.

The Amended Complaint alleged that the acquisition will likely substantially lessen competition for the sale of milk to schools in one hundred school districts in eastern Kentucky and Tennessee. On August 31, 2004, the District Court granted summary judgment to DFA and Southern Belle. The government appealed, and on October 25, 2005, the Court of Appeals reversed the grant of summary judgment as to DFA and remanded the case for trial. The Court of Appeals affirmed the dismissal of Southern Belle, leaving DFA as the only defendant. *See United States v. Dairy Farmers of America, Inc.*, 426 F.3d 850 (6th Cir. 2005).

On October 2, 2006, the government filed a proposed Final Judgment that requires DFA to divest its interest in Southern Belle and use its best efforts to require its partner, the Allen Family Limited Partnership ("AFLP"), to divest its interest in Southern Belle. DFA proposed divesting its interest and AFLP's interest in Southern Belle to Prairie Farms Dairy, Inc. ("Prairie Farms"), and the government approved Prairie Farms as a suitable buyer of DFA's and AFLP's interests in Southern Belle.

The government and DFA have stipulated that the proposed Final Judgment may be entered after compliance with the Tunney Act. Entry of the proposed Final Judgment would terminate this action, except that the Court would retain jurisdiction to construe, modify, or enforce the provisions of the proposed Final Judgment and to punish violations thereof.[1]

[1] Prairie Farms and DFA executed a purchase agreement for Southern Belle's assets on October 2, 2006. In keeping with the United States' standard practice, the proposed Final Judgment does not prohibit the completion of the divestiture before it is entered. *See* ABA Section of Antitrust Law, *Antitrust Law Developments* 387 (5th ed. 2002) (noting that "[t]he Federal Trade Commission (as well as the Department of Justice) generally will permit the

II. STANDARD OF JUDICIAL REVIEW

Upon the publication of the public comments and this Response, the United States will have fully complied with the Tunney Act and will move for entry of the proposed Final Judgment as being "in the public interest." 15 U.S.C. § 16(e), as amended. In making the "public interest" determination, the Court should apply a deferential standard and should withhold its approval only under very limited conditions. *See, e.g., Mass. Sch. of Law at Andover, Inc. v. United States*, 118 F.3d 776, 783 (D.C. Cir. 1997). Specifically, the Court should review the proposed Final Judgment in light of the violations charged in the complaint. *Id.* (quoting *United States v. Microsoft Corp.*, 56 F.3d 1448, 1462 (D.C. Cir. 1995) ("*Microsoft*")).

Before entering the proposed Final Judgment, the Court is to determine whether the Judgment "is in the public interest." 15 U.S.C. § 16(e). The Tunney Act states that, in making that determination, the Court may consider:

> (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

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underlying transaction to close during the notice and comment period"). Such a prohibition could interfere with many time-sensitive deals, prevent or delay the realization of substantial efficiencies, and delay effective relief.

> consideration of the public benefit, if any, to be derived from a determination of the issues at trial.

15 U.S.C. § 16(e)(1).

The United States described the courts' application of the Tunney Act public interest standard in the Competitive Impact Statement filed with the Court on October 2, 2006.

III. SUMMARY OF PUBLIC COMMENTS AND RESPONSES

During the sixty-day comment period, the United States received four comments from dairy farmers in Kentucky, one comment from a former Southern Belle employee, one comment on behalf of a cooperative of dairy farmers in Kentucky, and one anonymous comment. These comments are attached in the accompanying Appendix. After reviewing the comments, the United States continues to believe that the proposed Final Judgment is in the public interest.

A. Southeast Graded Milk Producers Association

Southeast Graded Milk Producers Association ("SEGMPA"), a cooperative of dairy farmers in Kentucky, submitted a comment which both thanked the government for challenging DFA's acquisition of its interest in Southern Belle, and expressed concerns about DFA's raw milk procurement practices. SEGMPA has been a long-time supplier of raw milk to Southern Belle. When SEGMPA tried to re-negotiate its supply contract with Southern Belle in 2006, Southern Belle decided not to renew the contract. SEGMPA then negotiated an agreement to supply raw milk to the Flav-O-Rich dairy in London, Kentucky. Flav-O-Rich is owned by National Dairy Holdings ("NDH"), which itself is 50%-owned by DFA. Shortly after the contract negotiations with Flav-O-Rich concluded, Flav-O-Rich told SEGMPA that it could not

go through with the supply contract, since DFA is the raw milk supplier to NDH's dairies, including Flav-O-Rich. According to SEGMPA, this left it with no outlet for its members' raw milk other than Southern Belle. SEGMPA went back to Southern Belle, and although it was able to negotiate a new raw milk supply contract, it was on much less favorable terms than it had previously negotiated. SEGMPA is concerned that in the future it will not be allowed to compete with DFA for raw milk supply contracts at Southern Belle, and urges that the government ensure that there is competition for raw milk as well as for school milk.

SEGMPA acknowledges in its comment that these raw milk concerns are different from the harm to competition for school milk alleged in the Amended Complaint and addressed by the proposed Final Judgment. While the government brought this case to protect competition in the market for the sale of milk served by schools in Kentucky and Tennessee, SEGMPA's concerns are about a different market, *viz.* the sale of raw milk to dairy processors like Southern Belle and Flav-O-Rich. Under the Tunney Act, however, a court's public interest determination is limited to whether the government's proposed Final Judgment remedies the violations alleged in its Amended Complaint. A review of the market for raw milk, which was not at issue in this litigation, would be inappropriate because it would construct a "hypothetical case and then evaluate the decree against that case," something the Tunney Act does not authorize. *Microsoft*, 56 F.3d at 1459.

B. Carl Phelps

A former Southern Belle employee, Carl Phelps, submitted a comment expressing concerns about the effect of the divestiture on the market for raw milk in Kentucky. As a Southern Belle employee, Mr. Phelps was the plant's contact with the dairy farmers that supplied

Southern Belle with raw milk and the haulers that transported the milk from the farms to the Southern Belle plant in Somerset, Kentucky. When SEGMPA negotiated a milk supply contract with Flav-O-Rich as a result of Southern Belle's decision not to renew its raw milk supply contract with SEGMPA, Mr. Phelps resigned from Southern Belle and joined Flav-O-Rich as a liaison between the plant and SEGMPA's members. Shortly after the contract negotiations with Flav-O-Rich concluded, Mr. Phelps was told that the contract between Flav-O-Rich and SEGMPA would not be finalized.

Mr. Phelps's first concern is that, in the future, Prairie Farms will not contract with SEGMPA for Southern Belle's raw milk, but instead choose to supply the plant with raw milk from its own members or DFA. This would effectively leave SEGMPA no customers for its members' raw milk, forcing SEGMPA to fold and its members to either join DFA or Prairie Farms. Mr. Phelps is concerned about these alternatives because he understands that SEGMPA's members have approached Prairie Farms about joining that co-op, but have been turned down. If SEGMPA were to shut down, Mr. Phelps contends that DFA would be the only outlet for SEGMPA's former members and would be able to reduce prices paid to farmers because it would have no competition.

This concern about competition in the market for raw milk is not related to competition in the markets for school milk at issue in this case. Mr. Phelps, like SEGMPA and other commentors expressing concerns about competition in the market for the sale of raw milk, does not argue that the proposed Final Judgment is not "within the reaches of public interest." Nor do they contest that because of their concerns about the market for raw milk, the divestitures required by the proposed Final Judgment will not remedy the competitive harm alleged in the

Amended Complaint. Rather, Mr. Phelps and these other commentators raise competitive issues in markets separate and distinct from those relevant to this matter.

Mr. Phelps's second concern is that, despite the divestiture of Southern Belle to Prairie Farms, DFA still may be able to influence Southern Belle's behavior in the school milk markets at issue because DFA and Prairie Farms are joint venture partners in the Roberts Dairy, Hiland Dairy, and Turner Dairy. He suggests that a third party monitor Prairie Farms to ensure that its operation of Southern Belle is totally independent of DFA, and that Southern Belle will compete with dairies partially owned by DFA, such as Flav-O-Rich.

Mr. Phelps's concern that joint ventures between Prairie Farms and DFA will affect Prairie Farms' operation of Southern Belle was considered by the government when evaluating Prairie Farms as a potential purchaser of Southern Belle. The government believes that the joint ventures will not undermine the proposed relief for several reasons.

First, these joint ventures involve dairies located in completely different geographic markets than those in which Southern Belle competes for school milk contracts. The Roberts and Hiland dairies, both 50%-owned by Prairie Farms and DFA, are located in Arkansas, Iowa, Kansas, Missouri, Nebraska, and Oklahoma. In addition, Prairie Farms recently acquired a partial ownership interest in the Turner dairy, which has plants in Arkansas, Kentucky, and Tennessee, and is 20%-owned by DFA. Turner's Kentucky plant is in Fulton, on the far western edge of the state, and does not compete against Southern Belle for school milk contracts.

Second, because these joint ventures involve different markets, Prairie Farms will not have the same incentive to lessen competition between Southern Belle and Flav-O-Rich (or any other DFA-affiliated dairy) that led to the filing of this case. The government challenged DFA's

acquisition of a 50% ownership interest in Southern Belle because DFA's partial ownership of both Southern Belle and Flav-O-Rich created a substantial incentive to reduce competition between those two dairies. The acquisition of Southern Belle by Prairie Farms has eliminated that common ownership between those two dairies. In the future, Prairie Farms will have a strong incentive to compete to obtain school milk contracts for its Southern Belle dairy at the expense of Flav-O-Rich. The dairies jointly owned by Prairie Farms and DFA do not compete for school milk contracts with Southern Belle, so Prairie Farms will not be able to reduce competition for school milk between Southern Belle and any of those dairies.

Third, the government evaluated and approved Prairie Farms as a buyer of Southern Belle because it has a demonstrated ability to operate dairy processors and compete for school milk contracts independent of any influence or control by DFA. Prairie Farms, as an agricultural cooperative of dairy farmers, has an economic incentive to supply its processing plants with raw milk from its members, so it is not dependent on DFA for its raw milk supply to its wholly owned processing plants. Its dairies compete for school milk contracts, and there is no evidence that it competes less effectively in geographic markets where it competes against processing plants partially owned by DFA.

Finally, the proposed Final Judgment protects against DFA's ability to exert control over Southern Belle. Section XI of the proposed Final Judgment prohibits DFA from reacquiring, directly or indirectly, any ownership interest in Southern Belle. As a result, if Prairie Farms transferred the assets of Southern Belle to one of its joint ventures with DFA, DFA would be in violation of the proposed Final Judgment. The government reviewed the terms of the proposed sale to Prairie Farms, and is confident that DFA will not retain any control over Southern Belle.

If the government learned of any agreement prohibited by the proposed Final Judgment, pursuant to Section X it could inspect DFA's records and request reports from DFA regarding its compliance. Similarly, this Court retains jurisdiction under Section XII of the proposed Final Judgment to enforce the proposed Final Judgment and punish any violations. For these reasons, the government believes that Mr. Phelps's suggested modification to the proposed Final Judgment is not warranted.

C. William R. Sewell and Bill L. Guffey

William R. Sewell and Bill Guffey, two dairy farmers from Kentucky, submitted comments raising the concern that the competition for raw milk in Kentucky could be lessened if SEGMPA is not able to supply Southern Belle with raw milk. As is the case with Carl Phelps's concerns about the market for raw milk, the concern expressed by Messrs. Sewell and Guffey does not address a violation alleged in the Amended Complaint, nor does their concern question whether the proposed Final Judgment remedies the harm alleged in the Amended Complaint.

D. Bradley J. Marcum

Bradley J. Marcum, a dairy farmer from Alpha, Kentucky, submitted a comment expressing concerns about the raw milk purchasing practices for Southern Belle after its divestiture to Prairie Farms. He notes that Prairie Farms has retained many of Southern Belle's key employees, and suggests that, therefore, DFA still influences Southern Belle's decisions.

To the extent that Mr. Marcum's comment suggests that the adequacy of the divestiture of Southern Belle to Prairie Farms as a remedy to the Amended Complaint's allegations is undermined by Prairie Farms' retention of Southern Belle's employees, the government disagrees. Permitting Southern Belle's new owner to retain the plant's existing employees

allows it to maintain the plant's customer accounts and keep its operations running smoothly with minimal interruption. The continued efficient operation of the Southern Belle dairy during the transition to a new owner was the reason why Section IV.F of the proposed Final Judgment was included. This section expressly allows a purchaser of Southern Belle to retain the plant's employees. Section IV.F also requires DFA to "not interfere with any negotiations by the Acquirer to employ any employee whose primary responsibility is the production, sale, marketing or distribution of products from the Southern Belle Dairy." By retaining employees who have been responsible for Southern Belle's operations, marketing, and sales, but who no longer have any connection to DFA, Southern Belle is better able to compete against Flav-O-Rich and other processing plants for school milk and other accounts.

E. Ronald Patton

Ronald Patton, a dairy farmer and past-president of SEGMPA, submitted a comment expressing concerns that other parties were not allowed to purchase DFA's interest in Southern Belle, including a local group of potential investors who wished to operate the Southern Belle plant independent of DFA or any other processing company. Mr. Patton is concerned that Prairie Farms' purchase from DFA of Southern Belle and its 2006 purchase from DFA of Turner Dairies indicates that other parties were foreclosed from bidding on Southern Belle.

As described in Section IV of the proposed Final Judgment, DFA was required to inform "any potentially qualified purchaser making inquiry regarding a possible purchase of the [Southern Belle dairy] that such assets are being offered for sale," and provide information about Southern Belle to all potential purchasers. The government, pursuant to Section IX.B-E of the proposed Final Judgment, received periodic updates on the inquiries DFA received from parties

interested in purchasing Southern Belle, and the status of DFA's negotiations with those interested parties. Based on these updates, the government is aware that DFA received multiple offers to buy Southern Belle.

The proposed Final Judgment does not require DFA to accept a particular offer, only that any acquirer of Southern Belle meet the conditions set out in Section IV.H(1)-(2). These provisions require Southern Belle to be sold to a purchaser who "has the intent and capability (including the necessary managerial, operational, technical and financial capability) of competing effectively in school and fluid milk markets in Kentucky and Tennessee, . . . [and] that none of the terms of any agreement between [the purchaser] and DFA give DFA the ability to act unreasonably to raise the [purchaser's] costs, to lower the [purchaser's] efficiency, or otherwise to interfere with the ability of the [purchaser] to compete effectively." The government reviewed information from both DFA and Prairie Farms regarding the purchase of Southern Belle and the presence of Prairie Farms in school milk markets in Kentucky and Tennessee. As noted earlier, Prairie Farms owns and operates multiple dairy processing plants elsewhere in the country, and has the knowledge and expertise to operate the Southern Belle Dairy efficiently, including the dairy's school milk business. It also has the capacity to supply its dairies with raw milk independent of DFA, whether through its own members or through other suppliers such as SEGMPA. The purchase agreement between Prairie Farms and DFA has no terms or conditions that would adversely affect the costs, efficiencies, or ability of Southern Belle to compete effectively for school and fluid milk sales. Based on this information, the government approved Prairie Farms as a buyer of Southern Belle because it met the requirements of Section IV.H(1)-(2) of the proposed Final Judgment.

F. Anonymous

The United States received an anonymous comment expressing the opinion that DFA agreed to sell Southern Belle to Prairie Farms because the sale would somehow allow DFA to eliminate SEGMPA as a competitor for raw milk contracts, and that Prairie Farms would refund the purchase price of the Southern Belle dairy back to DFA through some type of rebate mechanism. This commentor provides a lengthy history of Southern Belle, and suggests that DFA divested Southern Belle to Prairie Farms because it negotiated a side deal with Prairie Farms to have the new owner take steps to force SEGMPA out of business. The commentor, however, did not provide any evidence of such an agreement.

This comment's concerns about the market for raw milk, like other comments discussed earlier, are not germane to the evaluation of the conduct alleged in the Amended Complaint and addressed by the proposed Final Judgment. The government has no evidence of a side agreement between Prairie Farms and DFA relating to the sale of Southern Belle. If there were credible evidence of such an agreement, the government could investigate any potential violations of the proposed Final Judgment pursuant to its inspection rights in Section X of the proposed Final Judgment, and if it believed any provisions of the proposed Final Judgment were violated, Section XII of the proposed Final Judgment allows this Court to fashion an appropriate remedy.

IV. CONCLUSION

After careful consideration of the public comments, the United States concludes that entry of the proposed Final Judgment will provide an effective and appropriate remedy for the antitrust violations alleged in the Amended Complaint and is therefore in the public interest. Accordingly,

after publication of this Response in the *Federal Register* pursuant to 15 U.S.C. § 16(b) and (d), the United States will move this Court to enter the Final Judgment.

Dated: February 7, 2007

Respectfully Submitted,

/s/ Ihan Kim

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CERTIFICATE OF SERVICE

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