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IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

UNITED STATES OF AMERICA,

Plaintiff,

v.

PEARSON plc
PEARSON INC., and
VIACOM INTERNATIONAL INC.

Defendants.

No. 1:98CV02836
(Antitrust)

Filed: December 10, 1998

COMPETITIVE IMPACT STATEMENT

The United States, pursuant to Section 2(b) of the Antitrust Procedures and Penalties Act ("APPA"), 15 U.S.C. § 16(b) - (h), files this Competitive Impact Statement relating to the proposed Final Judgment submitted for entry in this civil antitrust proceeding.

I.

NATURE AND PURPOSE OF THE PROCEEDING

On November 23, 1998, the United States filed a civil antitrust Complaint alleging that the proposed acquisition by Pearson plc and its wholly owned subsidiary, Pearson Inc. (collectively "Pearson"), of certain publishing businesses of Viacom International Inc. ("Viacom") would violate Section 7 of the Clayton Act, 15 U.S.C. § 18. The Complaint alleges that Pearson and Viacom, two of the nation's largest publishers of textbooks and other educational materials, compete head-to-head in the development, marketing, and sale of comprehensive elementary school science programs and in the development, marketing, and sale of textbooks used in thirty-

two college courses. Unless the acquisition is blocked, competition for these science programs and college textbooks would be substantially lessened, leading to higher prices, a reduction in the value of materials or service provided to teachers and students, or lower quality. The request for relief in the Complaint seeks: (1) a judgment that the proposed merger would violate Section 7 of the Clayton Act; (2) a permanent injunction preventing consummation of the merger agreement; (3) an award of costs to the plaintiff; and (4) such other relief as the Court may deem just and proper.

Shortly before the Complaint was filed, the parties reached a proposed settlement that permits Pearson to complete its acquisition of Viacom's publishing businesses, yet preserves competition in the markets in which the transaction would raise significant competitive concerns. Along with the Complaint, the parties filed a Stipulation and proposed Final Judgment setting out the terms of the settlement.

The proposed Final Judgment orders Pearson to divest either its or Viacom's existing elementary school science program, along with the program that that party is currently developing, to an acquirer acceptable to the United States. Unless the United States agrees to a time extension, Pearson must complete this divestiture within two months of the filing of the Complaint, or within ten days of the expiration of the sixty-day statutory notice-and-comment period that commenced with the publication of this Competitive Impact Statement, whichever is later. The proposed Final Judgment also orders Pearson to divest fifty-five college textbooks so that competition in the development, marketing, and sale of textbooks in each of the thirty-two courses will be preserved. Pearson must complete the college textbook divestitures within five

months of the filing of the Complaint, or within ten days of the expiration of the sixty-day statutory notice-and-comment period, whichever is later.

If Pearson does not complete the divestitures within the appropriate time periods, the Court, upon application of the United States, is to appoint a trustee selected by the United States to complete the remaining divestitures. The proposed Final Judgment also requires Pearson and Viacom to take all steps necessary to maintain and market the products to be divested as independent and active competitors until the divestitures mandated by the proposed Final Judgment have been accomplished.

The plaintiff and defendants have stipulated that the Court may enter the proposed Final Judgment after compliance with the APPA. Entry of the proposed Final Judgment would terminate this action, except that the Court would retain jurisdiction to construe, modify, or enforce provisions of the proposed Final Judgment and punish violations thereof.

II.

DESCRIPTION OF THE EVENTS GIVING RISE TO THE ALLEGED VIOLATION

A. The Defendants and the Proposed Transaction

Pearson Inc. is a Delaware corporation headquartered in New York City, that publishes textbooks and other educational materials under such names as Addison Wesley, Scott Foresman and Harper Collins. Its parent, Pearson plc, is an international media corporation incorporated in the United Kingdom and based in London.

Viacom, a Delaware corporation based in New York City, publishes textbooks and other educational materials under names including Prentice Hall, Silver Burdett Ginn, and Allyn & Bacon. Its parent, Viacom Inc., is one of the world's largest entertainment and publishing companies and is a leading competitor in nearly every segment of the international media marketplace.

On May 17, 1998, the defendants signed an agreement under which Pearson would acquire educational, professional, and reference publishing businesses from Viacom. This transaction, which would increase concentration in already concentrated markets, precipitated the government's suit.

B. Product Markets

1. Basal Elementary School Science Program Market

a. Description of the Market

Most elementary schools throughout the United States teach science through comprehensive science programs known as "basal elementary school science programs," which provide organization and structure, as well as guidance and support, in how to teach the subject. Student textbooks and teacher's editions of the textbooks are the core of most basal programs, but most also include other important educational materials and services called "ancillary" materials, consisting of student workbooks and notebooks, audio-visual aids such as charts and videotapes, and materials for student science exercises and experiments. Basal elementary school science programs also often include services such as teacher training sessions.

School districts or individual schools desiring to purchase basal elementary school science programs would not turn to any alternative product in sufficient numbers to defeat a small but significant increase in the price of these programs or a reduction in the value of ancillary materials and services provided with them. For example, a school seeking to purchase a basal elementary school science program would not respond to a price increase by considering basal programs in mathematics or reading. Nor would schools substitute any of the few nontraditional, alternative science programs in sufficient numbers to defeat a small but significant price increase in basal elementary school science programs.

b. Harm to Competition as a Consequence of the Merger

Pearson and Viacom are two of only four large publishers of basal elementary school science programs. They have consistently led the market, capturing a combined share of roughly fifty percent or more of new sales over the last six years. Pearson's *Discover the Wonder* program is a close substitute for Viacom's *Discovery Works* program. Pearson and Viacom also compete to maintain and improve program quality. Both are currently developing new basal elementary school science programs that they will offer for sale throughout the United States beginning in 1999.

Pearson and Viacom's aggressive competition has led to lower prices, more and better ancillary materials and services, and improvements in product quality. The proposed acquisition would eliminate this competition and would further concentrate an already highly concentrated market.

Successful entry into the basal elementary school science program market is difficult, time consuming, and costly. A publisher would need to assemble an editorial and sales staff to develop, test, and market the new program, and would need to overcome schools' reluctance to purchase an elementary school science program from a firm lacking an established reputation as an experienced and reliable science publisher. Additionally, the science market is less attractive to new entrants because elementary school science funding is neither as large nor as reliable as it is for core subjects like math and reading.

The Complaint alleges that the transaction would likely have the following effects:

a. actual and future competition between Pearson and Viacom would be eliminated;

b. competition generally in the market for basal elementary school science programs would likely be substantially lessened;

c. prices for basal elementary school science programs would likely increase or the value of ancillary materials or services would likely decline; and

d. competition in the development and improvement of basal elementary school science programs would likely be substantially lessened.

2. College Textbook Markets

a. Description of the Markets

College professors generally select a textbook to serve as the primary teaching material for their course. Textbooks provide the core written material for a course, serve as the foundation for the professor's overall lesson plan, and set forth the framework for class discussions. Although it is the professor that chooses the textbook, students purchase the textbooks, usually from a college bookstore.

Publishers often attempt to induce a professor to select their textbooks by offering free ancillary educational materials such as a teacher's edition of the textbook, audio-visual teaching tools, and copies of the textbook for teaching assistants. Publishers also sometimes offer textbooks to students as part of discounted packages that include further ancillary educational materials such as CD-ROMs and study guides.

The Complaint identified thirty-two college courses in which Pearson and Viacom were among the leading competitors in the provision of textbooks and related educational materials. These courses primarily fell within the disciplines of biological sciences, engineering, economics, teachers' education, mathematics and computer science. In each of these courses, textbooks are used as the primary teaching materials. A small but significant increase in the price of a textbook for a college course -- or a small but significant decrease in the value of the ancillary materials provided with the textbook -- would not cause a significant number of professors or students to switch to any alternative products. Used textbooks also cannot defeat an increase in price of new textbooks or a decrease in the supply of ancillaries provided with them. The supply of used textbooks is limited, and professors usually require use of the newest edition of a textbook, which is generally revised every three to four years.

b. Harm to Competition as a Consequence of the Merger

In each of the thirty-two college textbook markets identified in the Complaint, Pearson and Viacom compete vigorously by offering textbooks that are close substitutes. Together, they account for a major share of new textbook sales, and face significant competition from only a small number of other publishers.

Competition between Pearson and Viacom has resulted in lower prices, more and better ancillary materials for professors and students, and improved product quality. The proposed acquisition would eliminate this competition, give Pearson the ability to raise the price or reduce the value of materials, and would further concentrate these already highly concentrated markets.

In each of the thirty-two college textbook markets, there is unlikely to be timely entry by any company offering textbooks and ancillary materials that would be sufficient to defeat an anticompetitive increase in price or decrease in ancillary materials. Successful entry involves a costly and time-consuming process in which a publisher must locate an author qualified to write a new textbook, and assemble an editorial staff to edit and develop the textbook. In addition, it must have numerous professors to review the textbook and a large sales staff to market it. Entry is also impeded by the difficulty of challenging the reputation of successful incumbent textbooks.

The Complaint alleges that the transaction would likely have the following effects:

a. actual and future competition between Pearson and Viacom would be eliminated;

b. competition generally in the markets for the sale of textbooks and ancillary materials for each of the college courses identified in the Complaint would likely be substantially lessened;

c. prices for textbooks and ancillary materials for each of the college courses identified in the Complaint would likely increase or the value of ancillary materials would likely decline; and

d. competition in the development and improvement of college textbooks and ancillary materials in each of the college courses identified in the Complaint would likely be substantially lessened.

III.

EXPLANATION OF THE PROPOSED FINAL JUDGMENT

The proposed Final Judgment is designed to eliminate the anticompetitive effects of Pearson's proposed acquisition of publishing businesses from Viacom.

The proposed Final Judgment requires divestiture of either Pearson's or Viacom's basal elementary school science program to an acquirer acceptable to the United States within two months after the filing of the proposed Final Judgment in this matter, or within ten days after the expiration of the sixty-day statutory notice-and-comment period that commenced with the publication of this Competitive Impact Statement in the Federal Register, whichever is later. This divestiture includes all textbooks or other educational materials offered for sale or provided or under development that refer or relate to the subject matter of science for elementary school grades, including, but not limited to (1) student editions; (2) teacher editions; (3) supplemental materials, including but not limited to workbooks, notebooks, charts, audio, video, software, CD-ROM, Internet and broadcast components, manipulatives and equipment, and similar materials; (4) teacher support and staff development materials, including, but not limited to teacher resource books, assessment materials and answer keys, test generators, teaching guides, overhead transparencies, lesson plans and outlines and curriculum materials; and (5) any other materials in any form, format or media marketed or intended to be marketed as being ancillary to the program or to an individual title within the program.

Pearson also must divest the fifty-five college textbooks identified on Exhibit B to the proposed Final Judgment. That exhibit specifies the one or more textbooks in each course that must be divested to ensure that each college textbook market suffers no reduction in competition. The college textbook divestitures must be completed within five months after the filing of the proposed Final Judgment in this matter, or within ten days after the expiration of the sixty-day statutory notice-and-comment period, whichever is later. Until the divestitures take place, Pearson is required to develop and maintain its and Viacom's products as independent, ongoing, economically viable, and active competitors, and to continue to fund their development, promotional advertising, sales, marketing, merchandising, and support.

If Pearson fails to make the required divestitures within the applicable time periods, the Court will appoint a trustee selected by the United States to effect the divestitures. Pearson may select which basal elementary school science program the trustee will divest, so long as that program has been developed and maintained at a level sufficient to ensure its competitive viability. If the United States determines, in its sole discretion, that Pearson has not adequately developed and maintained that program's competitive viability, the trustee will sell the other program.

The proposed Final Judgment provides that defendants will pay all costs and expenses of the trustee. After the trustee's appointment becomes effective, the trustee will file monthly reports with the parties and the Court, setting forth the trustee's efforts to accomplish divestiture. At the end of six months, if the divestiture has not been accomplished, the trustee and the parties will have the opportunity to make recommendations to the Court, which shall enter such orders as appropriate in order to carry out the purpose of the trust, including extending the trust and the

term of the trustee's appointment.

The proposed Final Judgment takes steps to ensure that the acquirers of the divested products will be viable and effective competitors. The United States must be satisfied that the acquiring parties have the ability and intention to publish and market the divested products as viable, ongoing businesses. The proposed Final Judgment also directs Pearson to use all commercially practical means to enable the acquirer of the basal elementary school science program to hire the personnel primarily responsible for the program's editorial content, including editors, authors, and science experts, and to encourage and facilitate their employment by the acquirer. Prior to divestiture, Pearson also may not transfer any of these employees to new positions within the company. The proposed Final Judgment also requires that Pearson provide acquirers with information about the employees responsible for the editorial content of the college textbooks to be divested, and about the employees primarily responsible for the production, design, layout, sale or marketing of *all* of the divested products. The proposed Final Judgment forbids Pearson and Viacom from interfering with any acquirer's employment negotiations with those employees, and from transferring some of these employees -- those spending the predominant portion of their time on a divestiture product -- to new positions prior to the divestitures.

The proposed Final Judgment requires sale of all the tangible and intangible assets that make up each divestiture product. It expressly defines each divestiture product to include all associated intellectual property, licenses, contracts, artwork, promotional and advertising materials, customer lists, and research data. The intellectual property specifically includes the

titles of all existing products to be acquired, but not trademarks or trade names that refer to Pearson or Viacom. Exhibit A of the proposed Final Judgment identifies in detail the specific items (including student editions, teacher editions, and ancillary materials) that are included within the basal elementary school science program that Pearson must divest. It provides, however, that Pearson may continue to use the divested basal elementary school science program to the extent necessary to fulfill its or Viacom's obligations under existing contracts with purchasers. These obligations consist mainly of the provision of replacement copies of consumable workbooks or lost or damaged textbooks. The proposed Final Judgment requires that the acquirer grant Pearson a royalty-free license so that it may continue to use the divested basal elementary school science program for this limited purpose.

The proposed Final Judgment is thus designed to maintain the present level of competition in the market for basal elementary school science programs and in the thirty-two college textbook markets identified in the Complaint by replacing the competitor eliminated as a result of the merger with one or more that is equally effective. It accomplishes this goal by requiring prompt divestitures so that the acquirer has adequate time to participate in the significant upcoming sales opportunities in schools and colleges, by providing the acquirer with an opportunity to employ the personnel that are critical to the success of the divested products, and by requiring divestiture of all tangible and intangible assets that make up each of those products.

IV.

REMEDIES AVAILABLE TO POTENTIAL PRIVATE LITIGANTS

Section 4 of the Clayton Act, 15 U.S.C. § 15, provides that any person who has been injured as a result of conduct prohibited by the antitrust laws may bring suit in federal court to recover three times the damages the person has suffered, as well as costs and reasonable attorneys' fees. Entry of the proposed Final Judgment will neither impair nor assist the bringing of any private antitrust damage action. Under the provisions of Section 5(a) of the Clayton Act, 15 U.S.C. § 16(a), the proposed Final Judgment has no *prima facie* effect in any subsequent private lawsuit that may be brought against defendants.

V.

PROCEDURES AVAILABLE FOR MODIFICATION OF THE PROPOSED FINAL JUDGMENT

The United States and defendants have stipulated that the proposed Final Judgment may be entered by the Court after compliance with the provisions of the APPA, provided that the United States has not withdrawn its consent. The APPA conditions entry upon the Court's determination that the proposed Final Judgment is in the public interest.

The APPA provides a period of at least sixty days preceding the effective date of the proposed Final Judgment within which any person may submit to the United States written comments regarding the proposed Final Judgment. Any person who wishes to comment should do so within sixty days of the date of publication of this Competitive Impact Statement in the Federal Register. The United States will evaluate and respond to the comments. All comments will be given due consideration by the Department of Justice, which remains free to withdraw its

consent to the proposed Judgment at any time prior to entry. The comments and the response of the United States will be filed with the Court and published in the Federal Register. Written comments should be submitted to:

Mary Jean Moltenbrey
Chief, Civil Task Force
Antitrust Division
United States Department of Justice
325 Seventh Street, N.W., Suite 300
Washington, DC 20530.

The proposed Final Judgment provides that the Court retains jurisdiction over this action, and the parties may apply to the Court for any order necessary or appropriate for the modification, interpretation, or enforcement of the Final Judgment.

VI.

ALTERNATIVES TO THE PROPOSED FINAL JUDGMENT

The United States considered, as an alternative to the proposed Final Judgment, a full trial on the merits against Pearson and Viacom. The United States is satisfied that the divestiture of the assets specified in the proposed Final Judgment will facilitate continued viable competition in the market for basal elementary school science programs and in the thirty-two markets for college textbooks identified in the Complaint. The United States is satisfied that the proposed relief will prevent the merger from having anticompetitive effects in these markets. The divestitures required by the proposed Final Judgment will preserve the structure of the markets that existed prior to the merger and will preserve the existence of independent competitors.

VII.

STANDARD OF REVIEW UNDER THE APPA
FOR PROPOSED FINAL JUDGMENT

The APPA requires that proposed consent judgments in antitrust cases brought by the United States be subject to a sixty-day comment period, after which the court shall determine whether entry of the proposed Final Judgment "is in the public interest." In making that determination, the court *may* consider --

> (1) the competitive impact of such judgment, including termination of alleged violations, provisions for enforcement and modification, duration or relief sought, anticipated effects of alternative remedies actually considered, and any other considerations bearing upon the adequacy of such judgment;
>
> (2) the impact of entry of such judgment 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.

15 U.S.C. § 16(e).

As the Court of Appeals for the District of Columbia Circuit held, the APPA permits a court to consider, among other things, the relationship between the remedy secured and the specific allegations set forth in the government's complaint, whether the decree is sufficiently clear, whether enforcement mechanisms are sufficient, and whether the decree may positively harm third parties. *See United States v. Microsoft*, 56 F.3d 1448 (D.C. Cir. 1995).

In conducting this inquiry, "the Court is nowhere compelled to go to trial or to engage in extended proceedings which might have the effect of vitiating the benefits of prompt and less

costly settlement through the consent decree process."[1] Rather,

> absent a showing of corrupt failure of the government to discharge its duty, the Court, in making its public interest finding, should . . . carefully consider the explanations of the government in the competitive impact statement and its responses to comments in order to determine whether those explanations are reasonable under the circumstances.

United States v. Mid-America Dairymen, Inc., 1977-1 Trade Cas. ¶ 61,508, at 71,980 (W.D. Mo. 1977).

Accordingly, with respect to the adequacy of the relief secured by the decree, a court may not "engage in an unrestricted evaluation of what relief would best serve the public." *United States v. BNS, Inc.*, 858 F.2d 456, 462 (9th Cir. 1988), *quoting United States v. Bechtel Corp.*, 648 F.2d 660, 666 (9th Cir.), *cert. denied*, 454 U.S. 1083 (1981). Precedent requires that

> [t]he 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. The court is required to determine not whether a particular decree is the one that will best serve society, but whether the settlement is '*within the reaches of the public interest.*' More elaborate requirements might undermine the effectiveness of antitrust enforcement by consent decree.[2]

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[1] 119 Cong. Rec. 24598 (1973). *See also United States v. Gillette Co.*, 406 F. Supp. 713, 715 (D. Mass. 1975). A "public interest" determination can be made properly on the basis of the Competitive Impact Statement and Response to Comments filed pursuant to the APPA. Although the APPA authorizes the use of additional procedures, 15 U.S.C. § 16(f), those procedures are discretionary. A court need not invoke any of them unless it believes that the comments have raised significant issues and that further proceedings would aid the court in resolving those issues. *See* H.R. 93-1463, 93rd Cong. 2d Sess. 8-9, reprinted in (1974) U.S. Code Cong. & Ad. News 6535, 6538.

[2] *United States v. Bechtel*, 648 F.2d at 666 (internal citations omitted) (emphasis added); *see United States v. BNS, Inc.*, 858 F.2d at 463; *United States v. National Broadcasting Co.*, 449 F. Supp. 1127, 1143 (C.D. Cal. 1978); *Gillette*, 406 F. Supp. at 716. *See also United States v.*

The proposed Final Judgment, therefore, should not be reviewed under a standard of whether it is certain to eliminate every anticompetitive effect of a particular practice or whether it mandates certainty of free competition in the future. Court approval of a final judgment requires a standard more flexible and less strict than the standard required for a finding of liability. "[A] proposed decree must be approved even if it falls short of the remedy the court would impose on its own, as long as it falls within the range of acceptability or is 'within the reaches of public interest.' (citations omitted)."[3/]

VIII.

DETERMINATIVE DOCUMENTS

There are no determinative materials or documents within the meaning of the APPA that were considered by the United States in formulating the proposed Final Judgment.

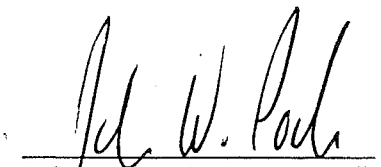
American Cyanamid Co., 719 F.2d 558, 565 (2d Cir. 1983).

[3] *United States v. American Tel. & Tel. Co.*, 552 F. Supp. 131, 150 (D.D.C. 1982), *aff'd sub nom. Maryland v. United States*, 460 U.S. 1001 (1983), *quoting Gillette*, 406 F. Supp. at 716; *United States v. Alcan Aluminum, Ltd.*, 605 F. Supp. 619, 622 (W.D. Ky. 1985).

FOR PLAINTIFF UNITED STATES OF AMERICA:

Dated: December 10, 1998

Respectfully submitted,



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