ly you don't understand what sells volume in the soft drink industry. So let me tell you, it is not just price. You can have the lowest price in the world. If you can't get the product delivered, if you can't get the display, you can't keep the display properly priced and stocked, then the price becomes insignificant." Summers, Tr. 7117-19.[87] Other evidence similarly confirmed the importance of the services involved in DSD delivery for increasing the volume of soft drink sales.[88]

In addition, the DSD delivery system also makes deliveries to smaller outlets economically feasible.[89] Such outlets, while having a relatively small direct volume effect, are important for image[90] and permit sampling that can lead to later sales.[91]

3. The Importance of Advertising

Branded CSD bottlers and concentrate companies invest significantly in advertising and promotion of their products. Concentrate

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[87] Other CCSW documents indicate the same view. When CCSW considered developing a "house" control brand to compete with private label, its analysis recommended use of DSD over a broker system for several reasons:

1. DSD gives us an opportunity to reach more channels convenience stores, mom & pops, mass merchandisers, etc. without increasing our costs dramatically. It also establishes an image and consumer sampling point of difference versus other private labels.

2. DSD allows us more flexibility to respond to changes in the marketplace (*i.e.*, lack of Coke ad feature activity, high volume hurdles, packaging emphasis changes, competitive features, etc.).
RX 398 D.

[88] *See* Section IV.B *supra.*

[89] Use of a warehouse-delivered system of distribution limits a firm to the large retail chains. Turner, Tr. 941. As a result, warehouse-distributed products cannot gain access to retail outlets such as drug stores, convenience stores, and smaller retailers that do not have the capacity to store the product. CX 3921 at 355 [Currie]; Turner, Tr. 941; CX 3943 at 15 [Rapp]; CX 3944 at 3511-12 [Rapp]; Coyne, Tr. 3438, 3445. Even CCSW admitted that "private/warehouse brands are less available in other market segments, including convenience stores, vending and fountain." RPFF paragraph 332 (citing Knowles, Tr. 2662, 2892).

[90] CCSW's president testified that presence in the fountain segment is important to develop the consumer's image of a product. Summers, Tr. 6513-14.

[91] Mr. Clements explained that Dr Pepper was not able to reach all of the types of outlets that they wanted to reach with warehouse delivery in Indianapolis and Los Angeles: "We were only able to get the people like the chains, and not all of them, and some of the independents like IGA that had a warehouse that could deliver. What we couldn't reach were the outlets we needed most, and that's the single drink sales -- the moms and the pops and the cafes and beauty shops and places like that. We did not have enough availability to create any great sampling of the product in order to develop the brand." CX 3582 at 2236 [Clements]. *See also* RX 398 D. Sampling occurs largely through cold drink sales rather than take-home sales. Turner, Tr. 1028-29.

firms pay millions of dollars annually in total marketing funding.[92] Huge amounts of monies, in the aggregate and as a percentage of total marketing, are spent by concentrate firms in support of local branded CSD bottler activities. For example, the largest component of Pepsi Cola total cost is allocated to marketing.[93]

With respect to advertising by retail stores, major retailers typically run two types of carbonated soft drink promotions: "ad features" and "in-store promotions." An ad feature is typically a newspaper advertisement featuring a branded CSD at an attractive reduced price, often at or below cost.[94] An in-store promotion typically involves a branded CSD in-store display also featuring a reduced price, though not usually as low as the ad feature price and without any accompanying newspaper advertisement.[95]

An ad feature may give a bottler 10 times the non-featured sales volume[96], while an in-store display may give just twice to 2 ½ times the normal sales volume.[97] The volume lift is much lower on the in-store display in part because the retail price to the consumer is usually higher.[98] Thus, bottlers are willing to pay thousands to hundreds of thousands of dollars to obtain ad features.[99] Bottlers also offer and pay large dollar amounts in order to have exclusive promotion and advertisement for their branded CSDs.[100] For example, CCSW's 1988 Calendar Marketing Agreement with Diamond Sham-

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[92] Turner, Tr. 965.

[93] CX 3913 at 38 [Drewes].

[94] CX 3806 Z50; Turner, Tr. 973-74; Davis, Tr. 4515 (at or below cost ads are termed "hot ads"); Gonzaba, Tr. 2032.

[95] Turner, Tr. 1126.

[96] Bodnar, Tr. 1498; Davis, Tr. 4504; Koch, Tr. 1831-32. Consumers also tend to stock-up during ad features, depending on the attractiveness of the ad feature price. Bodnar, Tr. 1766.

[97] Bodnar, Tr. 1498.

[98] Bodnar, Tr. 1498; Turner, Tr. 974; E. Hoffman, Tr. 362-63. Increased sales volume due to an ad promotion or reduced price end-aisle display is known in the industry as volume "lift." E. Hoffman, Tr. 358, 362.

[99] Turner, Tr. 1129-30.

[100] CX 1040 A-F (Pepsi); CX 1041 A-K (Grant-Lydick); CX 1042 A-V (CCSW).

rock stated that "[n]o national brand soft drink may be co-featured during these promotional periods."[101]

Ad features are run as part of retailers' promotional "ad cycles," which include bottlers, branded CSDs as part of the advertising.[102] Most major chain retailers advertise one branded CSD in each of their weekly ads during a 52-week cycle.[103] Major convenience stores usually offer a monthly ad cycle.[104]

Bottlers believe that you cannot grow your brands without being in the ad cycle.[105] In fact, some believe that if a bottler never gets an ad feature, the effect will be volume deterioration in the marketplace.[106] Nor can the lost volume necessarily be made up for through in-store displays.[107]

There are promotional periods that are more advantageous than others. Holiday periods are the most advantageous and create considerable volume lift.[108] For that reason, a retailer's holiday ad features cost hundreds of thousands of dollars for bottlers and concentrate firms.[109] Additionally, to obtain such ads from a retailer, the bottler must provide a greater discount than normal on its product.[110] Retail-

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[101] CX 1039-B. Pursuant to Calendar Marketing Agreements ("CMAs"), the bottler and retailer agree to a schedule of promotional activities and the payments to be made to the retailer. CMAs were originally developed to help the retailer offset the cost of advertisements for their chain stores. Davis, Tr. 4506. CMAs usually involve a base payment by the bottler to a retailer for a set number of ads. There are additional incentive payments for incremental volume growth. The bottler and retailer agree to sales projections and various requirements. CMAs are also known as "soft drink agreements," or "ad buy" agreements, "ad assistance," or "volume incentives." Davis, Tr. 4509, 4706; Gonzaba, Tr. 2055; Hiller, Tr. 5355.

[102] Turner, Tr. 970.

[103] Turner, Tr. 970; Davis, Tr. 4526; Kaiser, Tr. 3177.

[104] E. Hoffman, Tr. 362.

[105] Turner, Tr. 974; CX 3941 at 288-89 [Schmid].

[106] CX 3941 at 288-89 [Schmid].

[107] Turner, Tr. 974.

[108] Turner, Tr. 971; Summers, Tr. 6919; Davis, Tr. 4514-16. The July 4th ad is usually considered the most valuable, followed by other summer holidays, then the Thanksgiving, Christmas and New Year's holiday periods. Turner, Tr. 971; E. Hoffman, Tr. 367-68; Turner, Tr. 4514. As to non-holiday ad periods, pay week periods are more valuable than non-pay week ads. Turner, Tr. 971; E. Hoffman, Tr. 368; Davis, Tr. 4514.

[109] Summers, Tr. 6919. For example, the holiday ads of H.E.B., a very large retailer in the San Antonio area (and other areas in Texas), run from a low of $175,000 for Easter to a high of $500,000 for summer holiday ads. Summers, Tr. 6919; Gonzaba, Tr. 2055.

[110] Gonzaba, Tr. 2057. However, there is a safety net of $50,000 for holiday ads if volume falls short. Summers, Tr. 6918-19.

ers, such as H.E.B., must meet volume requirements in order to receive the ad payments in full.

Bottlers also compete with each other for retail space in retail outlets which sell branded CSDs.[111] Bottlers attempt to convince retailers that their branded CSD products will generate sufficient traffic to warrant display space and end-aisle displays.[112]

D. Branded CSDs as a Relevant Product Market

With this background information in place, we can now properly address the question that the parties have presented to us: whether beverages other than branded CSDs could constrain a price increase by branded CSDs in the relevant geographic market. For this inquiry, we examine all of the relevant evidence concerning price and non-price competition that could affect the likelihood that nonbranded CSDs would constrain a small but significant, nontransitory price increase by branded CSDs. Such evidence includes the opinions of market participants concerning price and advertising differences among different categories of soft drinks, historical evidence of price interactions among different categories of soft drinks, and industry perceptions about the degree of competition between different categories of soft drinks.

As we will discuss, nonbranded CSDs are largely unavailable in the cold drink channel.[113] Therefore, we will focus in particular on the likely substitution responses if branded CSD bottlers in the relevant geographic market raised their prices to retailers in the take-home channel, who purchase branded CSDs for sale to the ultimate consumer.[114] The retailer typically receives a discount or allowance off the wholesale list price in return for its promotion of the product.[115] "Net price" charged to the retailer equals the list price minus

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[111] CX 4005 at 55 [R. Hoffman].

[112] CX 4005 at 55-56 [R. Hoffman].

[113] *See* Section IV.D.2 *infra*.

[114] The Merger Guidelines advise that "[i]n general, the price for which an increase will be postulated will be whatever is considered to be the price of the product at the stage of the industry being examined." Section 1.11. The same sentence appears in the 1984 Guidelines.

[115] For example, in 1990, at least 95% of CCSW's sales were made at less than list price. Summers, Tr. 6721. Only 2% of the sales of the Pepsi COBO in the San Antonio area were made at list price. Davis, Tr. 4684-85. *See also* RX 327.

discounts and allowances.[116] "Net/net" or "net/net/net" prices are list prices minus discounts, allowances, and ad payments.

It is also relevant here to examine the likely substitution responses if retailers raised the prices of branded CSDs to consumers, since the demand for the bottlers' products derives from consumer demand for those finished products.[117] Some agreements between bottlers and retailers regarding advertising funds attempt to influence the retailer to offer a certain price to consumers for the finished product, a further indication of the interrelationship between prices to retailers and prices to consumers.[118]

For the reasons set forth below, we find that the evidence demonstrates a relevant product market of branded CSDs.

1. Overall Substitution Possibilities: Views of Branded SD Bottlers

Both of CCSW's primary branded CSD competitors in the San Antonio area stated that if branded CSD bottlers in San Antonio raised their prices by 10%, and everything else remained constant, they could profitably raise their price by 10%.[119] Bottlers of branded CSDs in other South and Central Texas areas gave similar responses.[120] This evidence was uncontroverted.[121]

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[116] R. Hoffman, Tr. 5652-53; Summers, Tr. 6713-14; CX 414 B.

[117] The Merger Guidelines state that, among other evidence, the Commission may take into account "the influence of downstream competition faced by buyers in their output markets" in evaluating market definition. Section 1.11.

[118] Promotional allowances are usually related to a performance requirement. This most commonly takes the form of a feature ad, in-store display, or a reduced retail price. CX 1039 B, C; CX 1041 H ("lowest retail price on featured package"). Although bottlers do not usually suggest retail prices, they often set discounts at levels calculated to drive a desired retail price, based on the margin usually added by a particular retailer. Campbell, Tr. 1972-73. In addition, when soft drinks are in a feature ad, retailers often add little or no margin to the wholesale price, or use incremental funding from the bottler to further reduce the retail price. Turner, Tr. 960, 973-74. As explained by Mr. E. Hoffman, "[w]hat we're really trying to have happen is for the retailer to pass the cost, the lower cost, on to the consumer so that the benefit of the consumer -- the lower price is to induce more consumption or purchases." E. Hoffman, Tr. 380.

[119] Bodnar, Tr. 1492, 1496, 1762-63; Davis, Tr. 4610.

[120] Koch, Tr. 1815-16; Turner, Tr. 988-89; CX 3931 at 1801-04 [Westerman].

[121] Respondent CCSW argues that this testimony is not probative because complaint counsel did not specify a time frame for the hypothetical price increase. ABR-A at 8. An example of the testimony elicited by complaint counsel is given by Mr. Davis, a Pepsi official:

Q. If Coke SW and Big Red raised their prices ten percent in San Antonio, would Pepsi find it profitable to raise its prices the same?

The internal documents of the three bottlers of branded CSDs in the San Antonio area confirm that they take into account ~~only~~ the prices of other branded CSD products in deciding on pricing for their own branded CSD products. CCSW's own business records indicate that CCSW does not consider the price of private label or warehouse-delivered soft drinks when it considers increasing the price of its branded CSDs.[122] Rather, CCSW considers the prices of other branded CSDs in determining the price of its branded CSDs.[123]

Moreover, CCSW's business records characterize its major competition as limited to manufacturers, distributors, and sellers of branded CSDs.[124] CCSW markets its branded CSDs against other branded CSDs.[125]

A. Yes, they would.
Davis, Tr. 4610.

As discussed above, the hypothetical "5%" price increase test is set forth in the Merger Guidelines, which typically define a small but significant and "nontransitory" price increase as a 5% price increase maintained for a year or more. Section 1.11. Although we agree that complaint counsel could have clarified the precise implications of this question by specifying a time frame, we do not find that the absence of a specified time frame renders such testimony worthless. "Profit" is generally understood as the gain still left after expenditures; this is not a short-run concept, but rather something that businesses typically calculate over a time frame of months or years, not days. Thus, we believe that the question implied a "nontransitory" time frame. In any case, the witnesses' responses indicate that the answer may well have been the same whether a short or long time frame had been specified, since no witness asked "Do you mean in the short run or the long run?" Finally, we note that this is just one piece of the evidence supporting a branded CSD product market definition. We interpret the responses to complaint counsel's questions in light of that surrounding evidence, the weight of which also supports a branded CSD product market.

[122] CX 2244; CX 198; CX 3101 C-H, J; CX 3102 B-H, J, L.

[123] CX 104 D, G, H, M-N; CX 198.

[124] CX 418 Z2-3, Z9, Z12, Z16, Z20; CX 1406 Z9-10; CX 1854 H-I, K-L, T-U, X, Z2-5, Z7-8; CX 1866 K-L. For example, CCSW's records reveal that it viewed Mr. PIBB as the closest substitute to and a direct competitor of Dr Pepper. CX 596 A-I. Indeed, that CCSW recognizes the difference between branded and nonbranded CSDs is well-evidenced by their consideration of a proposal to establish a house product flavor line in the take home segment that would fill the gap between branded CSDs and private label. The proposal was to "[i]ntroduce a DSD house line of flavors to include a Cola, Cherry Cola, Red, Rootbeer, and Orange. The line should be positioned as an image product with a low price (slightly higher than the private labels). Image development can be achieved through quality graphics, package availability, broad channel distribution and a unique trademark (perhaps the Buck Brand label)." RX 398. This document is consistent with other CCSW documents that express concern that CCSW needed a flavor line to compete with an expanding private label market. *See, e.g.*, RX 2059; RX 2060; RX 226 A, K; CX 2974 Q, R.

[125] CX 3760 ("In summary, beat the hell out of Pepsi!"); CX 104; CX 108 H; CX 1854 R,U, Z2, Z4; CX 2255 S, T; CX 3109 C. Messrs. R. Hoffman and Summers, Tr. 6853, testified that CCSW's branded CSDs compete in a broad sense with virtually all liquids (*See, e.g.*, R. Hoffman, Tr. 5524: CCSW competes with water in the sense that all beverages vie for the same shelf space), but CCSW documents do not evidence the same approach.

CCE bottlers in Texas, Coke-Austin and Coke-Houston, create periodic reports in which they monitor the activities of their competitors. Such activities -- which include pricing, package availability, marketing activities, sales, market share and pricing strategies -- are generally limited to observing the activities of bottlers of branded CSDs.[126] Similarly, the bottling operations of CCE use Keystone reports that provide information only with regard to branded CSDs.[127]

When Coke-Austin introduced diet Coke, its introductory plans included volume and share forecasts. These projections were limited to branded CSDs and did not include private label or warehouse soft drinks.[128] When Coke-Austin did a competitive analysis entitled "Competitive Corporate Brands," it discussed only branded CSDs.[129]

Pepsi official Davis testified that at the bottler level, Coke products are the only products to which the Pepsi bottler in San Antonio would react with regard to price.[130] "... Coke [CCSW] is usually the leader in the market. They go up and then we usually follow, depending on our pricing structure."[131] Davis stated that Pepsi does not follow private label CSDs closely enough to know whether they had price increases.[132]

Pepsi bottler-related testimony and documents evidence a similar distinction between branded CSDs and nonbranded CSDs. For example, Pepsi official Davis testified that Pepsi would not be worried about promoting its products in conjunction with private labels, but would not want Pepsi jointly marketed with Coke.[133] When the Pepsi COBO bottler serving the San Antonio area performs comparisons with its competitors, it looks in detail to bottlers of branded

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[126] CX 2689; CX 2690; CX 2691; CX 2693.

Some documents note an increasing private label market share (*e.g.*, CX 2623 F, CX 2561 N, O, Q), but very few suggest a price response from branded CSDs to such brands, and this evidence is much weaker than that pointing in the opposite direction. In one exception, an SWCC employee apparently suggested that a response to private label brands was necessary to forestall the "expense of regaining price leadership long term." RX 1479 J.

[127] CX 2680; CX 2688 A-D; CX 2695; CX 2918.

[128] CX 503 B-J.

[129] CX 171.

[130] Davis, Tr. 4532-33.

[131] Davis, Tr. 4532; CX 441 C; CX 445 H-I, K; CX 448; CX 449 R-S.

[132] Davis, Tr. 4531, 4829.

[133] Davis, Tr. 4824.

CSDs for their pricing and other competitive activity,[134] as well as the "ad feature" or in-store allowances and ad assistance that they are offering.[135]

Emery Bodnar, former General Manager of DPSA and current Executive Vice President, General Manager and part owner of Grant-Lydick, similarly testified that Grant-Lydick considers and reacts only to prices of other branded CSDs in setting Grant-Lydick's branded CSD prices, and does not consider the prices of private label or warehouse-delivered soft drinks in setting branded CSD prices.[136]

Other bottlers also consider and react only to prices of the products of branded CSD bottlers in their areas when setting the prices of

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[134] CX 455 G-L, Z-24; CX 456 B-C; CX 457 C; CX 458 B; CX 459 E; CX 460 I; CX 461 J, L; RX 1013 U-W; CX 380. At least one document notes that, in 1989, private label's market share had increased at the expense of Pepsi. RX 1287 E. Mr. Davis of Pepsi COBO explained that this followed the deep discounting of 1987-88, when branded CSD prices had become so low that they were "taking share out of private label." Davis, Tr. 4528-29. When the branded CSD prices went back up, however, then you still have "the price shopper that's going to pick up private label," and so "you're losing share back to the private label." Davis, Tr. 4528-29. *See also* Section IV.D.3.d *infra*.

[135] RX 1013 J-Y; CX 455 H-I, K, Z-1, Z-3; CX 456 E, F; CX 457 C, F; CX 458 G.

[136] Bodnar, Tr. 1359-61, 1364, 1490, 1492-94, 1762-63.

Emery Bodnar, as manager of the Big Red bottler in San Antonio, explained why he would not lower Big Red's price to retailers if a warehouse or private label lowered its price 10%:

Q. Let me ask you this question. If Texas Beverage Packers lowered its triple net price in the ten-county area including and surrounding San Antonio ten percent and all other things remain constant, again for a sustained period of time, would you find it profitable to lower your prices?

A. I don't know what Texas Beverage Packers' triple net price is. I wouldn't know if they lowered it or not. See, because that doesn't come through the same channel as we do.

We're a direct store and they're through warehouses and through, you know, private label.

Q. Let's assume you did know.

A. If I did know that they went down ten percent?

Q. Yes.

A. Would I do anything? No.

I've got to -- Let me just, if I can, state why.

Private label or control brands, at least from where I sit, are not direct competition, as I look at Coke and Pepsi in San Antonio and maybe whatever they're calling themselves today, Premiere. Okay?

Those brands that are essentially the warehouse or private label, first of all, space is dictated by somebody at headquarters and we're not going to change that.

Number two, the product is displayed by somebody in the store or has to be handled by somebody in the store.

If you really go out and look at beverage sections, most often than not if you look at a beverage section that looks ragged, it is the section that is supposed to be controlled by store personnel.

As far as display space, that is pretty much, again, dictated, not at store level but at some buyer's level or higher.

So really, there's not much I can do to compete, if I really wanted to. I mean, it's there, just the same say that Kool-Aid is, as we talked about earlier.

So if he lowered his price 15, 20 percent, I wouldn't do anything. Fifty percent. He doesn't have that kind of margin to do it, but if he did.

They just can't execute. I mean, they just don't have the force to execute such a thing.

Bodnar, Tr. 1762-63.

their branded CSDs.[137] Moreover, bottler collusion cases indicate that branded CSD bottlers in other geographic areas believe that it is possible to raise price successfully together without having to involve bottlers of nonbranded CSDs.[138]

2. Substitution Possibilities: The Cold Drink Channel

In the cold drink channel, which includes fountain, vending machine, and single drink sales[139] there is relatively little availability of nonbranded CSDs that is, warehouse-delivered and private label CSDS. Respondent admitted that warehouse delivered brands are generally not available in the cold drink channel,[140] and stated that "private/warehouse brands are less available in other market segments, including convenience stores, vending and fountain."[141] The evidence confirms that warehouse distribution does not provide access to the vending and fountain channels.[142]

In addition, the evidence shows that carbonated soft drinks sold in vending machines are almost entirely brands that are direct-store-door delivered, not warehouse-delivered or private label brands.[143] Vending machines are stocked with nationally branded CSDs, with virtually no private label brands available.[144] Moreover, although private label brands may be marginally more available in the fountain channel, since a few restaurant chains sell certain flavors as their own private label brands,[145] the record does not establish that the occasion-

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[137] Trebilcock, Tr. 5844-46, 5848-50; Davis, Tr. 4532-33; CX 3990 at 923 [Kalil].

[138] As we discuss in Section VI.C.3 *infra*, we find the bottler collusion cases relevant to this case, and we therefore find that the ALJ erred in excluding evidence relating to them. For the cases cited by complaint counsel (*See* Section VI.C.3.c *infra*), warehouse-delivered and private label firms in areas where branded CSD bottlers have been convicted of fixing prices were not named as defendants. The price-fixing cases involved only branded CSD bottlers.

[139] *See* Section IV.B *supra*.

[140] RRCCPFF paragraph 876.

[141] RPFF paragraph 332, citing Knowles, Tr. 2662, 2892.

[142] RX 3005 at 3759 [Smith]; CX 3978 at 2063-64 [Lowenkron]; Turner,Tr. 941, 1403; CX 3945 at 177 [Rapp]; CX 3944 at 3511-12 [Rapp]; CX 3977 at 72 [Carew]; Coyne, Tr. 3438; CX 3942 at 1905 [Wilson].

[143] CX 804 G; CX 3989 at 65-66 [Shanks]; RX 3003 at 82-84 [Huey].

[144] Koch, Tr. 1835; Clarke, Tr. 4284; Turner, Tr. 1007; RX 3003 at 84 [Huey].

[145] Summers, Tr. 6517; Short, Tr. 7759-60. For example, McDonald's sells its own orange private label fountain product. Short, Tr. 7759.

al presence of nonbranded CSDs in the cold drink channel would provide a constraint on the pricing of branded CSDs.

3. Substitution Possibilities: The Take Home Channel

The record shows that private label and warehouse brands are available in this channel. Therefore, we must examine in greater detail whether their presence would be sufficient to constrain a small but significant, nontransitory price increase in branded CSDs.

a. Views of Bottlers of Warehouse and Private Label

Texas Beverage Packers, Inc. ("TBP") is a manufacturer of private label and warehouse-delivered CSDs on its own account and for some of the major supermarkets in San Antonio.[146] Steve Hixon, its general manager, testified that his carbonated soft drinks do not compete with those of CCSW and San Antonio Pepsi,[147] and that to do so would render his company "dead meat."[148] He sees manufacturers and distributors of private label and warehouse-delivered CSDs as his direct competitors,[149] and not CCSW or Pepsi.[150] With respect to pricing, he reported the following:

Q. Now, in your opinion, there has not been an impact on your business by Coke Southwest's purchasing of the San Antonio Dr Pepper Bottling Company; is that correct?

A. Yes.

Q. Your basic opinion is we're dealing with apples and oranges in this case?

A. We're dealing with apples and oranges other than if there's some kind of pricewar going on. If they get down to 99 cents, then they do impact me, but I don't feel the -- If Coke had bought Pepsi, yes.

Q. And you feel that that's because -- You don't see a relationship between you and Coke Southwest because you basically sell to different clientele on different bases?

A. No. We're -- Well, we're sitting in a grocery store next to each other, but I don't -- For the people to take my product over Coca-Cola, there's got to be a substantial differential in price to make them select the private label.

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[146] Hixon, Tr. 7269.

[147] Hixon, Tr. 7354-57.

[148] Hixon, Tr. 7356.

[149] Hixon, Tr. 7359.

[150] Hixon, Tr. 7360.

Q. In fact, when you were first interviewed by FTC staff, you told them this doesn't have anything to do with you and you wish we'd leave you alone?
A. Absolutely. Still feel that way.

Hixon, Tr. 7354-55.

With respect to the "impact" when branded CSDs reduce their prices, Mr. Hixon explained:

Q. In your experience, have national brands gotten down to the level of private labels in their pricing?
A. They haven't gotten quite that low but it's been kind of -- They've gotten close enough to make it scary.
Q. Have they in fact begun to squeeze out private label with low prices?
A. That's a tough question. Certainly, to a limited extent, I think they have. When they get in their 99-cent a six-pack wars with cans, yeah, at that point they're driving out private label. It's so low.
We virtually have given up the major holidays to the national brands. We no longer try to compete with them.

Hixon, Tr. 7303.

Hixon views CCSW and Pepsi as "just out there screwing up the market with [their] occasional low prices." Hixon, Tr. 7360. He sees these bottlers as not trying to get his business, nor as having an impact on his business. Hixon, Tr. 7360-61. Hixon described himself and his "fellow copackers" as competing with branded CSDs only on the fringe:

[We are] out there scrambling over the ten percent of the business that Coke and Pepsi don't realize really exists or have slipped through their fingers, or whatever, that they choose to ignore. So yeah, if Coke or Pepsi drop their prices to 99 cents, it impacts our ten percent that we're fighting over. It takes business away from us.

Hixon, Tr. 7360.

The Kroger Company operates a CSD manufacturing plant in Garland, Texas, called Garland Beverage Company ("GBC").[151] GBC does not consider the prices of branded CSDs in determining the price of its private label and warehouse-delivered products. The record does not show such a comparison.[152] GBC monitors only other private label and warehouse-delivered soft drinks, such as

151 Morath, Tr. 7672-73.

152 RX 1716-17; RX 1721-22; RX 1726; RX 1740-41; RX 1744-45; RX 1750; RX 1754-57; RX 1760.

Rocky Top, Big K, Mega, Parade, and Cragmont.[153] GBC also monitors TBP.[154]

This evidence also supports the existence of a branded CSD product market. The weight of the testimony by and documentary evidence of bottlers of both branded CSDs and nonbranded CSDs indicates that branded and nonbranded CSDs generally do not compete in the sense that a branded CSD price increase could be constrained by nonbranded CSDs.[155] The evidence does establish that branded CSDs occasionally may constrain pricing by private labels and warehouse-delivered soft drinks, but it does not provide any reason to believe that nonbranded CSDs could constrain price increases by branded CSDs.[156]

b. Consumer Conduct: The Typical Price Gap Between Branded and Nonbranded CSD Retail Prices to Consumers

Prices of CSDs appear generally to fall into three separated groupings. Most expensive are the branded CSDs; less expensive are warehouse-delivered brands; and cheapest are the private label products.[157] The price gaps separating these groupings may indicate that these soft drinks are in different product markets.[158] Although the Commission and the courts do not always divide premium and

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[153] RX 1760 (991440; 991475-79; 991482-85); CX 2827 D, E.

[154] RX 1756; RX 1757.

[155] For example, Mr. Campbell, warehouse manager for a Pepsi/Dr Pepper/7-Up bottler in Halletsville, Texas, was asked whether he competed with H.E.B.'s Plaza brand with his Dr Pepper and Pepsi brands. Mr. Campbell responded: "Well, yes and no. I mean, not really. I mean, I don't -- I don't think about competing against those people. I mean, that's not who I go to look in the grocery store to see if they've reduced their price by one cent a can and then I adjust my pricing and my promotional strategies based upon that. I base my competing more against other direct store delivery products." Campbell, Tr. 2007. Even Mr. Howell of CCUSA admitted that he had never seen the price of Coke drop in response to private label prices. Howell, Tr. 4123. And Mr. Summers explained that CCSW created a private label to compete with private label and warehouse brands, being careful not to cannibalize CCSW's branded products. Summers, Tr. 696284.

[156] Similarly, Pepsi's research shows that it is very hard for a private label to steal from a national brand, but that a national brand can gain share from a private label temporarily if its price comes down low enough. CX 3912 at 65-66, 97 [Christiani].

[157] CX 814 E; CX 3989 at 92-93 [Shanks].

[158] *See, e.g., United States v. Archer-Daniels-Midland Co.*, 866 F.2d 246 (8th Cir. 1988), *cert. denied*, 493 U.S. 809 (1989) (despite functional interchangeability of sugar and high fructose corn syrup, persistent price difference of 10% to 30% resulting from price support system required treatment as separate product markets).

lower-priced brands into separate markets,[159] the existence of a price gap calls for some examination of its degree and possible significance.

We note first that the wholesale prices available to retailers vary, because bottlers may change their promotional offers on a weekly to monthly basis.[160] At any time, there may be a variety of effective wholesale prices for any given brand and package within any given geographic area.[161] Retail prices to consumers also vary frequently, depending on the extent to which and whether particular brands are on "promotion." The promoted prices of branded CSDs may be substantial discounts off the everyday or list retail price to consumers. The differences between the promoted retail prices of branded CSDs and the nonpromoted prices of branded CSDs vary from 20% to over 100%.[162]

Despite these variations in price differences, there are clear distinctions between the average prices of branded CSDs and non-branded CSDs, at both the wholesale and retail price level. As respondent CCSW has explained, the wholesale prices paid by the retailer for most private/warehouse brands generally are less than the price charged by the bottler for branded CSDs.[163] Much of this differential is attributable to the labor cost of stocking and merchandising the product, which is usually borne by the bottler using DSD delivery for branded CSDs, but by the retailer for private/warehouse brands.[164] An additional cost difference is that national concentrate companies often spend significant sums of money advertising and

[159] Coca-Cola Co., Dkt. No. 9207, slip op. at 32 n. 62; *see also Olin Corp.*, 113 FTC 400, 595-600 (1990), *aff'd*, 986 F.2d 1295 (9th Cir. 1993) (finding two relevant product markets, one consisting only of premium-priced product and one consisting of the premium-priced product and its functional equivalent), *cert. denied*, 114 S. Ct. 1051 (1994).

[160] Campbell, Tr. 1954; R. Hoffman, Tr. 5551-52; Summers, Tr. 6613-H. However, some retailers set their promotional schedule for an entire year at the beginning of the year. Summers, Tr. 6618.

[161] CX 1979; CX 2180; Turner, Tr. 1474; Bodnar, Tr. 1648-49; Davis, Tr. 4702-03; RX 1200; Kaiser, Tr. 3224.

[162] CX 3973 (20-100%); CX 3926 A (30-50%); CX 3832 (20%); CX 3835 (20%).

[163] Howell, Tr. 4028-29; RX 2423.

[164] CX 3700 J; Brinkley, Tr. 2191-92; Kaiser, Tr. 3159; Turner, Tr. 1401-02. *See also* Section IV.C.2 *supra*.

promoting their branded CSDs.[165] These costs are often reflected in a higher concentrate price to bottlers.[166]

Similarly, the average retail prices of most private/warehouse brands are less than the average retail prices of branded CSDs.[167] Estimates of the price differential vary, but a common estimate is that private/warehouse prices average between 20% to 30% below the prices of branded CSDs.[168] There was testimony that the retail price gap between branded CSDs and private label CSDs is normally two to three price points, per unit.[169] In 1984, CCUSA found that, on average, private and controllabels net retail prices were an average of 29% lower than those of the national brands, while warehouse-delivered Shasta/Faygo net retail prices were about 20% below the national brands.[170] In 1988, an analysis of the average case price differences for several bottler groups was performed, comparing Fanta, Shasta, Faygo, Controlled label and Coke Classic in 34 geographic areas.[171] The average case price difference between Coke Classic and the highest priced control label products was $0.94. Branded flavor lines were priced above control labels at an average price difference of $0.77 a case.[172]

This retail price gap shows that certain consumers are willing to pay more for branded CSDs than for private label or warehouse-delivered brands. Many consumers perceive a quality difference

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[165] CX 3158 Z11-Z21; CX 814 A-B. Most private label brands are not advertised on television or radio, but may appear in the retailer's newspaper ads or circulars. Some warehouse brands, notably Shasta, have engaged in television and radio advertising in the past. *See* Section IV.C.3 *supra*.

[166] Bodnar, Tr. 1739.

[167] Hixon, Tr. 7356-57; Trebilcock, Tr. 5841-42.

[168] Trebilcock, Tr. 5841-42; Howell, Tr. 4082; CX 3814 at 39 [Adams]; CX 814 at 874. At different times, the retail price gap between branded CSDs and private label/warehouse soft drinks may range from 10% to 130%, depending on whether special promotions are offered. Trebilcock, Tr. 5841-42 (20-30%); Hixon, Tr. 735657 (30-40%); CX 3989 at 89-90 [Shanks]; Bodnar, Tr. 1715-16; CX 3835; CX 3832; CX 3926B (20-70%); Limon, Tr. 4981 (6-pack ("6-pk") cans: private label CSD is 99 cents; Pepsi is $1.49 - $1.69 [49-69%]); Sendelbach, Tr. 7703-06 (6-pk cans: private label CSD is $1.20; branded carbonated soft drink is $1.59 [33%]); Brinkley, Tr. 2194-95 (6-pk cans: private label CSD is $1.20-$1.32; branded CSD is $2.50 [50%]); Chapman, Tr. 7208, 7211 (6-pk cans: private label CSD is $1.06-$1.26; branded CSD is $1.59 $2.00 [26-88%]); Davis, Tr. 4519-24.

[169] CX 3967 at 186 [Carew]. Each price point has significance for a bottlers' revenue; for example, for CCSW, a ten-cent increase in the net price of a six-pack can increase cash flow by an additional $8 million a year, holding all else constant. E. Hoffman, Tr. 284; CX 875 G.

[170] CX 814 A.

[171] CX 3436 S-Y.

[172] CX 3436 F.

between branded CSDs and private label/warehouse delivered CSDs.[173] Because of that perception, branded CSDs have greater consumer appeal than do private label/warehouse-delivered CSDs,[174] and brand switching by consumers is generally limited to branded products.[175]

The perceived differences in quality apparently account for the fact that branded CSDs have some degree of brand loyalty.[176] The extent of brand loyalty has decreased recently, and consumers more readily switch between branded CSDs if prices differ significantly; however, there is little evidence of switching from branded CSDs to private label/warehouse-delivered CSDS,[177] at least until the price differences are very large.[178] If the retail price of branded CSDs drops near or below the price of private/warehouse brands, then private/warehouse brands may lose sales to the branded CSDs.[179] Again, such evidence indicates that branded CSDs may constrain nonbranded CSD pricing on occasion, but not the converse.[180]

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173 Morath, Tr. 7676.

174 CX 3912 at 65-66, 97 [Christiani].

175 CX 3942 at 1911-12 [Wilson].

The ALJ concluded that branded and private label CSDs have similar functional characteristics, implying that they are in the same product market, although he acknowledged that "[t]o a great extent, any perceived differences among soft drinks exists in the mind." ID at 61. In evaluating the likelihood of customer switching in the event of a small but significant, nontransitory price increase, such perceptions in the mind are more relevant than a chemical test of whether the ingredients are basically the same.

176 CX 3967 at 205 [Carew]; Morath, Tr. 7676.

177 CX 3942 at 1911-12, 1940-41.

178 CX 3921 at 386-87.

Mr. Koch, President of Oneta Company, the Pepsi-Cola bottler in Corpus Christi, testified that, as to supermarkets only, "[w]e know that private labels have about a 10 percent residual share of the market that's based on existing price structures and existing price differences." Koch, Tr. 1876. He stated that "private labels do a lot to keep us honest," in the sense that "[g]o maybe 20 percent higher with a national brand than you can with private label, and then you start to lose volume." Koch, Tr. 1875. Other than the responses of branded CSD bottlers to the 5% question, *see* Section IV.D.1 *supra*, this is virtually the only piece of testimony that directly addresses whether private label could constrain upward pricing of branded CSDS. We do not find this testimony sufficient to outweigh the weight of the evidence related to this point, especially since Mr. Koch only states his belief that branded CSDs would lose volume to private label, but does not state that such losses would make it unprofitable for branded CSDs to raise price.

179 Bodnar, Tr. 1555-56; Summers, Tr. 6549 (branded CSD discount to $.99 will pick up some private label share, but "usual" discount of $1.49 does not); Hixon, Tr. 7303-04, 7360; Chapman, Tr. 7190; Turner, Tr. 988; Campbell, Tr. 1999; RX 3011 at 3171-78, 3197-98 [Skinner].

180 *Cf. Olin Corp.*, 113 FTC at 598-600 (lower-priced swimming pool chemical could not constrain upward price movement of premium-priced swimming pool chemical). *See also* Coca-Cola Co., slip op. at 36.

Indeed, the preponderance of the evidence concerning brand loyalty suggests that consumers may be reluctant to switch to nonbranded CSDs in the event of branded CSD price increases.

For purposes of product market definition, the relevant question is whether, if a wholesale branded CSD price increase were passed on as a retail price increase, consumers would switch to nonbranded CSDs and thereby force a rollback of the wholesale branded CSD price increase? The record contains a study designed specifically to address the issue of what magnitude of branded CSD price would cause consumers to switch to nonbranded CSDs, albeit in a different geographic market. When Procter & Gamble owned Coke-Mideast Bottling Company, it did an elasticity analysis, comparing warehouse-delivered CSDs and Coca-Cola products. It found that an acceptable spread between Coke products and Big K's private label products was between 80 and 100%. If the prices of Coke products were above this level, consumers' normal preferences for branded CSDs began to diminish.

> On the other hand, if the Coke was for sale for 99 cents and Big K was for sale for 95 cents, Big K didn't sell almost at all because the spread was so small, consumers would virtually all opt for Coca-Cola.

CX 3921 at 386 [Currie].

This study supports the conclusion that sales of nonbranded CSDs would not constrain a retail price increase to consumers of branded CSDs when the initial price gap is the average size that we observe -- that is, branded CSD prices averaging 20-30% above the prices for private/warehouse soft drinks.[181] Since the study indicates that consumers' preferences for Coke products would not diminish until the prices for Coke products were more than 80-100% above the prices for private label products, the study indicates that retailers most likely could pass along to consumers any 5% or other small but significant, nontransitory price increase by branded CSD bottlers. This ability would likely diminish the incentives of retailers to fight

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The ALJ cited testimony of Robert Chapman of H.E.B., a retailer, that his belief was that, if prices of branded CSDs decreased, sales of private labels would decrease. IDFF paragraph 216. That such substitution might occasionally occur, however, does not establish that if prices of branded CSDs generally increased, then sales of private label would increase sufficiently to make the price increase unprofitable for the branded CSDS.

[181] *See* note 168 *supra*.

such a price increase, since they would not have to absorb the price increase themselves.

c. Views of Concentrate Companies

Evidence from concentrate firms also is consistent with a product market confined to branded CSDs. CCUSA analyzes the market with regard to branded CSDS.[182] CCUSA performs business reviews of retail accounts in which it evaluates the performance of Coke products. In its 1988 H.E.B. business review, it listed the top ten brands of CSDs in both San Antonio and Austin; not one private label or warehouse brand was listed.[183] The 1990 Marketing Program presented to H.E.B. by CCUSA and Coca-Cola bottlers discusses and makes comparisons among only branded CSDs.[184] CCUSA generally has compared its prices of cherry Coke and Mr. PIBB only to Dr Pepper and not to any nonbranded CSD.[185]

PepsiCo as a concentrate company looks at the retail prices of only branded CSDs.[186] Pepsi performs periodic competitive analyses comparing Pepsi brands to CSDs of its competitors.[187] These studies generally do not involve private label CSDs.[188] Arthur Christiani,

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[182] CX 2547; CX 801; CX 803; CX 1892 L.

In the instances where CCUSA compared its products with nonbranded CSDS, the comparison involved a CCUSA product that diverges from the profile of a branded CSD. For example, CCUSA analyzes Fanta, which is not nationally advertised, in comparison to warehouse-delivered Shasta and private label brands. *See, e.g.*, CX 3436 B, C; RX 687 D, M; RX 958 B-D; CX 1084; CX 1991-Z31; Howell, Tr. 4029-31, 4023-25. In assessing whether to create a Fanta line of flavors, CCUSA believed that "[a] Fanta line would be unlikely to incur competition from Pepsi Cola USA," and that "Fanta cola would compete with Coke and Coca-Cola classic only on the fringe, and thus not have any significant negative effect on these two brands." CX 799 F. For CCUSA's branded CSDs, the documents reveal only infrequent references to concern about competition from private label and warehouse brands. *E.g.*, CX 169 C (concern that some Coke sales had been lost to private label or warehouse brands).

[183] CX 506 T, Q, U.

[184] CX 2263.

[185] CX 790 E; CX 791 M.

[186] CX 381 I. Concentrate companies subscribe to Nielsen's retail sales report service, which provides one collective entry for most private label and warehouse-delivered CSDs (except Shasta and Faygo). RX 694 at 13, 16; RX 2806. Concentrate firms do not subscribe to SAMI, which provides detailed analyses of the sales of warehouse-delivered brands, including CSDs. Clarke, Tr. 4279.

[187] CX 381.

[188] CX 3912 at 121 [Christiani].

Two documents have compared the profitability of DSD versus warehouse delivery for retailers and noted that, to compete with warehouse on price, it would be necessary for Pepsi to lower costs, since DSD costs more than warehouse delivery. CX 385 X to Z-53; CX 1922.

manager of business analysis for Pepsi, explained the process by which he performs retail elasticity studies for Pepsi.[189] Christiani concluded when a retailer promotes its private label CSDs it does not supplant purchases of Coke or Pepsi products.[190] He also concludes that, generally, "[i]t is hard for a private label brand to gain share from a national brand because of the types of consumer dynamics." CX 3912 at 65-66, 97 [Christiani].[191]

When Dr Pepper performs reviews of retail accounts, it does not compare the performance of Dr Pepper brands with private label or warehouse soft drinks.[192] Dr Pepper looks to Coke, Pepsi, 7-Up and RC products when comparing sales volume movements, not to those of private label and warehouse soft drinks.[193] During the period of time that Dr Pepper Company owned and operated production facilities, its review of these operations involved analysis of Dr Pepper products' performance with branded CSDs.[194]

The testimony of other market participants similarly confirmed that the pricing and marketing of branded CSDs is separate from that for non-branded CSDs. For example, A&W does not market its A&W brand products against private label products, nor does it develop marketing strategies with respect to private label products.[195] Michael Skinner of Shasta testified that increasing the price difference between his warehouse-delivered CSDs and DSD-delivered CSDs was not profitable,[196] that he saw little response by Pepsi or Coca-Cola to Shasta's prices,[197] and that he experienced price pressure from private label brands only in limited areas of the

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[189] CX 3912 at 139-40 [Christiani].

[190] CX 3912 at 70 [Christiani].

[191] Mr. Christiani testified that "a national brand can gain share from a private label brand temporarily if its price came down low enough." CX 3912 at 65-66 (emphasis added). This statement does not establish the converse, of course. Mr. Christiani stated that private labels on sale would typically cannibalize Pepsi only if private label were included in the top three brands in the market, which was not the case in the six markets he examined. CX 3912 at 24-27 [Christiani].

[192] CX 504; CX 206; CX 212 K-M; CX 214 H.

[193] CX 600; CX 836 J-Q; CX 2524; CX 2526; CX 834.

[194] CX 834; CX 2526.

[195] CX 3978 at 2096-97 [Lowenkron].

[196] RX 3011 at 3198-3201 [Skinner].

[197] RX 3011 at 3201 [Skinner].

country, not including Texas.[198] The testimony indicated that so-called 'boutique' firms such as Jolt Cola Co., Original New York Seltzer, Soho, Sundance and Snapple have no effect on the prices of branded CSDs.[199] The president of Double Cola stated that private label CSDs compete primarily with warehouse-delivered CSDs.[200]

The ALJ relied on evidence that the National Soft Drink Association includes a large variety of CSD and non-CSD beverages in its reports, and that government agencies put private labels with national brands in certain reports, as evidence of a product market broader than branded CSDs. ID at 61; IDFF paragraphs 205, 206. But neither the government's "SIC" categories nor the NSDA's categories track whether all of the items within each category could constrain price increases of the other items. We find the business records and testimony of market participants to be more probative of the relevant competitive issues and the weight of that evidence supports a product market confined to branded CSDs.

d. Pricing History and Price Patterns

(i) 1987-1990 Branded CSD Pricing in San Antonio and Other Areas

The history of price changes by branded CSD bottlers during the 1987-1990 time period also provides some insight into whether branded CSDs are a relevant product market. In contrast to the ALJ,[201] we find that this evidence supports the existence of a product market of branded CSDs.

In 1987, the Pepsi COBO significantly increased its discounts in its territories overall, starting in San Antonio in particular.[202] Pepsi official Davis explained that the Pepsi COBO became concerned because they had only a few ads scheduled for the year and feared a

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[198] RX 3011 at 3202 [Skinner].

[199] CX 3989 at 99-100, 169 [Shanks (Double Cola)]; CX 3941 at 320 [Schmid (7-Up)]; CX 3921 at 408 [Currie (Procter & Gamble)]; CX 3990 at 928 [Kalil (Kalil Bottling)]; RX 3014 at 3557-59 [Greenberg (Unadulterated Food Products)].

[200] CX 3989 at 93 [Shanks].

[201] The ALJ interpreted the evidence surrounding these price changes as supportive of a product market including non-branded CSDS. *See, e.g.*, IDFF paragraph 222; ID 60. As we will discuss, we believe that the ALJ's conclusion resulted from a misinterpretation of the evidence.

[202] Davis, Tr. 4527, 4548-59.

loss of volume if something was not done to compensate for the lack of ads.[203] They decided that, in San Antonio, they wanted to be "at least one, if not two, [price] levels below Coke," and that "[w]herever Coke went, we'd go a little lower."[204]

Davis stated that the Pepsi COBO serving San Antonio "led" pricing down in 1987.[205] According to Davis, during this period usually Pepsi would move its prices down first, and Coke would then match Pepsi's lower prices.[206] There was some variability in the direction of prices during this period. For example, in January 1988, Pepsi and CCSW raised prices.[207] Similarly, in March, 1988, Coke moved its pricing for cans back up, and Pepsi followed. However, during the summer of 1988, Pepsi led pricing back down.[208] Finally, in the fall of 1988, the price war abated when Pepsi led pricing back up.[209] This conduct was in contrast to Coke's usual position as price leader, which Mr. Davis described: "Coke is usually the leader in the market. They go up and then we usually follow, depending on our pricing structure."[210]

Davis described Pepsi's 1987-88 pricing as Pepsi's attempt to gain market share at the expense of losing money.[211] He stated that the Pepsi COBO probably gained about four share points as a result of the deep discounting,[212] but reported that the Pepsi COBO has found that it can "drive [its] business a lot easier" by bringing up prices and giving ad payments to retailers than by "trying to drive it just with price."[213] Since the Pepsi COBO wanted to become more

[203] Davis testified that Pepsi gains a "significant increase in volume" -- from 4 to 10 times the usual volume -- when an ad feature for Pepsi is on. Davis, Tr. 4504.

[204] Davis, Tr. 4548.

[205] Davis, Tr. 4527.

[206] Davis, Tr. 4550-59.

[207] Davis, Tr. 4557-58; Hilke, Tr. 5959.

[208] Davis, Tr. 4558-59.

[209] Davis, Tr. 4559. Overall, CCSW's San Antonio wholesale net/net/net prices (that is, net of discounts, allowances, and ad payments) increased 2.8% (from $6.11 to $6.28) between 1987 and 1988. CX 4114; RX 3085.

[210] Davis, Tr. 4532.

[211] Davis, Tr. 4560.

[212] Davis, Tr. 4564.

[213] Davis, Tr. 4528.

profitable, it has now adopted a strategy of working on getting ads and not dropping prices so low.[214]

Both the ALJ and CCSW rely heavily on two Pepsi documents,[215] stating that private label gained share at the expense of both Pepsi and Coke because of the 1988 price increases to show that branded and nonbranded CSDs are in the same product market. However, this reliance misses the point.

As Mr. Davis explained, private labels had lost share when branded CSD prices became so low during the deep discounting in 1987-88.[216] When branded CSD prices rose again, branded CSDs lost share back to the private labels because "you still have the price shopper that's going to pick up the private label."[217] Mr. Davis agreed that both Pepsi and Coke had taken "a volume hit" when branded CSD prices rose again,[218] but pointed out that, since Pepsi's Nielsen data include Big Red in the category of private label, "we're not really sure how much of it is Big Red and how much of it is private label."[219]

A resolution of whether Pepsi actually lost volume to private label instead of to Big Red is not necessary for disposition of this issue, however. The question is not simply whether a branded CSD price increase caused branded CSDs to lose share to private labels. Rather, the question is whether any loss of share made the price increases so unprofitable that Pepsi or Coke rescinded them. If no rollback of the price increases occurred, then one can assume that Pepsi and Coke found them profitable despite any loss of volume to private label, and that therefore their pricing was unconstrained by private label.

The testimony shows that whatever losses of volume to private label might, have occurred were insufficient to constrain price increases of branded CSDs in the San Antonio area in 1987-88 or in other, more recent times. Mr. Davis testified that Pepsi had no concern about possible volume losses to private label and that Pepsi

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[214] Davis, Tr. 4528. Davis testified that, although the Pepsi COBO has always lost money in the San Antonio area, it lost a lot more as a result of the deep discounting in 1987-88. Davis, Tr. 4561.

[215] *E.g.*, RX 2503 A.

[216] Davis, Tr. 4528-29.

[217] Davis, Tr. 4529.

[218] Davis, Tr. 4529.

[219] Davis, Tr. 4829-30.

had not rolled back any wholesale prices or increased any discounts to retailers in response to increased private label sales resulting from H.E.B. private label ads.[220] He noted that Pepsi had rolled back some wholesale price increases in 1990 due to competition with Coke, not because of private label price competition.[221]

Grant-Lydick's Big Red followed CCSW's pricing increase in 1989 as confirmed in an internal lender report which relates a conversation that the author of the report had with Toby Summers, CCSW's president, and David Green, CCSW's chief financial officer:

> Toby [Summers] and David [Green] analyzed month-by-month performance beginning with January, 1989.
> . . . In February, TBG implemented a 6% price increase at the wholesale level resulting in a 3% to 4% net price increase after discounts. Big Red matched the price increase immediately in mid-February. Pepsi matched the price increase on March 1.

CX 3806 Z56.

In addition, Mr. Bodnar of Grant-Lydick testified that if CCSW raises its prices, the convenience stores and independent stores will raise Big Red's retail prices to match CCSW's prices even if Grant-Lydick does not raise Big Red's wholesale prices. Thus, Mr. Bodnar's practice is to raise his prices when CCSW's increases its prices.[222] For example, in early 1990, CCSW raised the wholesale prices of certain of its package sizes, and Grant-Lydick maintained its same price levels. A month later Mr. Bodnar surveyed 100 accounts and found that:

> Our retails went up to match Coke's. So we had no choice but to raise our levels. I mean, the retailer was taking the long margin on us.

Bodnar, Tr. 1493.[223]

Although this evidence alone is not dispositive, it is overall supportive of the existence of a branded CSD product market.

[220] Davis, Tr. 4530-32, 4760.

[221] Davis, Tr. 4531-32.

[222] Bodnar, Tr. 1492-96.

[223] Some retailers testified that they would not raise the price of one branded CSD based on a price rise for another, *e.g.*, Gonzaba, Tr. 2106-07, but Mr. Bodnar's review of 100 accounts indicates that it can happen.

(ii) Price Relationship Studies

When the prices for two products move in different directions over time, it indicates that the products are in different antitrust product markets.[224] In this case, complaint counsel presented evidence attempting to show that prices for branded and non-branded CSDs have moved in different directions over time. We find, however, that complaint counsel's study is inconclusive and cannot be afforded much weight.

Complaint counsel's economic expert, Dr. Hilke, compared the relative net price movements of branded CSDs with those of private label and warehouse brands for 1987 through 1989.[225] For his analysis, he used a "sign test," which simply tests whether the prices moved in the same direction, but does not provide any information on the relative differences in magnitude of any price movements.[226] Using comparisons of quarterly data, Dr. Hilke found different direction price movements 2 times out of 10; using monthly data, he found different direction price movements 17 times out of 32.[227] Complaint counsel argues that these data show that branded and nonbranded CSDs are in different product markets, especially since the sign test does not take into account possible large differences in same direction price movements. By contrast, respondent's economic expert, Dr. Strickland, asserted, and the ALJ agreed, that the data show highly parallel price movements that are not random.[228]

Overall, we find that the price movement data is not particularly useful in resolving the product market question. Especially for branded CSDs, which are frequently sold on low-priced ad features, prices may change on a week-to-week basis; the unusually large swings in price attest to this.[229] Comparisons of monthly data, in our view, are overly sensitive to this problem.

Moreover, even assuming that this problem can be overcome by comparisons of quarterly (instead of monthly) data -- which is not

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[224] *See United States v. Aluminum Co. Of America*, 377 U.S. 271, 276-77 (1964); *see* generally Antitrust Law Developments (3d) at 285 (1992).

[225] CX 1678 A-D.

[226] Hilke, Tr. 5954.

[227] CX 1678 A-D.

[228] Strickland, Tr. 8060; IDFF paragraph 232.

[229] *See* Section IV.C.3 *supra*.

obvious to us -- and that the quarterly data show similar direction price movements, such nonrandomness can be caused for reasons other than that branded and nonbranded CSDs are in the same product market. For example, there is ample testimony that soft drink prices in general (as is true for many retail prices) are seasonal.[230] The prices of products in two different antitrust product markets could well exhibit some movements in the same direction simply because of seasonal price changes or holiday-oriented discounting. Such may well be the case here.

In sum, we do not rely on the price movement data because we believe they are unreliable and should be given little weight. In any case, the results are inconclusive and therefore do not add to the substantive analysis.

e. Views of Retailers

Evidence from retailers is consistent with a product market confined to branded CSDS. Trish Adams, the senior DSD buyer for all Target Corporation stores[231] testified that Target department stores have a limited amount of shelf space to dedicate to CSDs. Consequently, Target meets consumer demand head-on by offering only branded CSDs. This demand includes Big Red in San Antonio.[232] Even a 20% increase in branded CSD prices would not motivate Target to include private label CSDs in its beverage aisle.[233] When Target carried private label CSDs, branded CSDs were not affected by placing private label CSDs on sale.[234]

Circle K and 7-Eleven convenience stores had private label CSDs at one time, but discontinued them.[235] Mass merchandisers in San Antonio also do not carry the private label CSD, Texas Cola, because they only want branded CSDs.[236]

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[230] *See* Section IV.C.3 *supra*.

[231] CX 3814 at 5 [Adams].

[232] CX 3814 at 9-11 [Adams]. San Antonio is Big Red's largest market, and Grant-Lydick is the largest Big Red bottler. IDFF paragraph 85; Turner, Tr. 953.

[233] CX 3814-54 [Adams]. *See also* CX 3821-48 [Imper].

[234] CX 3814-36, 39-41.

[235] Howell, Tr. 4000; Knowles, Tr. 2892.

[236] Hixon, Tr. 7358-59.

4. Summary

We find that the weight of the evidence establishes the existence of a relevant product market limited to branded CSDs. With respect to the cross-elasticity of wholesale prices, there is consistent San Antonio bottler testimony that they could profitably raise branded CSD prices by 10%. Similarly, the documents and testimony of bottlers, concentrate companies, and retailers overall indicated that branded CSDs are priced in comparison to other branded CSDs, not private label or warehouse brands. With respect to retail pricing of finished products, the weight of the evidence demonstrated a persistent price gap between branded and non-branded CSDs, reflecting a premium that consumers are willing to pay for branded CSDs. There was no testimony or other evidence that retailers would be unable to pass along any cost increases for branded CSDs, thus possibly putting pressure on bottlers to refrain from price increases.

With respect to industry perceptions, the documents and testimony consistently supported significant distinctions between branded and non-branded CSDs in terms of prices, level of brand name recognition and advertising support, method of distribution, and availability in different channels of distribution. Thus, we conclude that the weight of the evidence shows a relevant product market of branded CSDs.

V. THE RELEVANT GEOGRAPHIC MARKET

Having determined the product market to be branded CSDs, we turn now to defining the geographic market, the second "necessary predicate" for analyzing an acquisition's effect on competition. *See United States v. Marine Bancorporation*, 418 U.S. 602, 618 (1974); *Brown Shoe Co. v. United States,* 370 U.S. 294, 324 (1962); *United States v. E.I. DuPont de Nemours & Co.*, 353 U.S. 586, 593 (1957). Such an inquiry is, of course, a prerequisite to determining whether the acquisition may result in a substantial lessening of competition in branded CSDs "in any section of the country" (Clayton Act Section 7, 15 U.S.C. 18). *See United States v. Marine Bancorporation,* 418 U.S. at 618.

Complaint counsel alleges that the geographic market within which to assess this acquisition consists of a ten-county area centered

around San Antonio, Texas (the "San Antonio market").[237] These ten counties comprised the original territory granted through the 1984 sale of the Dr Pepper franchise to CCSW. Respondent contends in response that the San Antonio market is inappropriately narrow, and suggests instead a far larger market that includes the major cities of San Antonio, Austin, Waco, Dallas, and Houston. *See* RX 2983. Although the ALJ ultimately failed to delineate a specific geographic market, he rejected the San Antonio market, finding that the relevant geographic market was larger than the ten-county area around San Antonio. *See* IDFF paragraph 245; ID 67.

For the reasons discussed below, we reject the ALJ's findings and conclude, based upon our own review of the record, that complaint counsel carried its burden of proving that the relevant geographic market is the San Antonio market. In reaching this conclusion, we note that the ALJ's geographic market evaluation was erroneous in several important respects. First and foremost, the ALJ's assessment must be disregarded because it was premised on an incorrect and unreasonably broad view of the product market as encompassing not only branded CSDs, but also private label and warehouse (non-branded) CSDs, mixers, seltzers, non-carbonated beverages (*e.g.*, Lipton Iced Tea), and isotonic drinks (*e.g.*, Gatorade). Second, the ALJ failed to apply the proper standard for defining a geographic market, as set forth in the Merger Guidelines, at Section 1.21, 4 Trade Reg. Rep. (CCH) paragraph 13,104 at 20,573.[238] *See* Adventist Health System/West, FTC Dkt. 9234 (Apr. 1, 1994), 5 Trade Reg. Rep. (CCH) paragraph 23,591 at 23,258. In addition, the ALJ gave undue weight to, and otherwise misapplied, the Elzinga-Hogarty test concerning shipping patterns.

Under Section 1.21 of the Merger Guidelines, the relevant geographic market is defined as the smallest region within which a hypothetical monopolist could "profitably impose at least a 'small but significant and nontransitory' increase in price, holding constant the terms of sale for all products produced elsewhere." The "profitably impose" language implicitly recognizes that, in the face of a price

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[237] This proposed market includes seven counties (Atascosa, Bandera, Bexar, Frio, Kendall, Medina, Wilson) and portions of three others (Blanco, Comal, and Karnes). IDFF paragraph 245.

[238] The approach to geographic market in the Merger Guidelines is essentially identical to that taken in Section 2.3 of the 1984 Merger Guidelines, 4 Trade Reg. Rep. (CCH) paragraph 13,103 at 20,558.

increase, some sales will inevitably be diverted elsewhere, as would be expected. Consequently, a geographic market will exist, notwithstanding some diversion of trade, so long as the additional profit from the price increase over the remaining customers exceeds the profit lost from the trade that was diverted.

In defining the geographic market using the methodology described in the Merger Guidelines, the Commission begins with the location of the merging firms and asks what would happen if a hypothetical monopolist imposed at least a "small but significant and nontransitory" price increase, typically 5% over a one-year period. If, in response to the price increase, the reduction in sales would be sufficiently large to render the price increase unprofitable, then the agency adds the next best substitute location to the proposed market, and the test is repeated. *See* Adventist Health-System/West, 5 Trade Reg. Rep. (CCH) paragraph 23,591 at 23,258.

The record contains direct evidence establishing that a hypothetical monopolist selling branded CSDs in the San Antonio market could profitably raise prices by more than 5% for a nontransitory period. Most significantly, branded CSD bottlers in the San Antonio market provided undisputed testimony to the effect that they could profitably -- and without fear of outside competition -- raise their prices by as much as 10% if other branded CSD bottlers in this market did the same.[239] Consistent with the foregoing evidence, bottlers of branded CSDs outside the San Antonio market testified that they would not ship into the San Antonio market, even if the price of branded CSDs in that market increased by 10%.[240]

Another consideration that directly bears upon the likely response to a price increase is the fact that competition in the local soft drink industry is characterized by the use of exclusive territories.[241] Concentrate firms grant bottlers exclusive rights (franchises) to manufac-

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[239] Bodnar, Tr. 1492, 1496, 1762; Davis, Tr. 4610; Koch, Tr. 1815-16; Turner, Tr. 995-96. Respondent argues that this testimony should be disregarded because the hypothetical question posed by complaint counsel failed explicitly to incorporate a one-year time frame. We disagree. Because the question was framed in terms of profitability (*see, e.g.*, Davis, Tr. 4610), we believe that this question was correctly understood by the witnesses as referring to a nontransitory price increase, *i.e.*, a price increase that would be maintained for more than an insignificant period of time. Consequently, we accept the responses as constituting probative evidence of the existence of a San Antonio market.

[240] Turner, Tr. 8598-99 ; Campbell, Tr. 1946-47; Van Houten, Tr. 8470-76; Koch, Tr. 8625-26; Davis, Tr. 4476-78; Bodnar, Tr. 1712-13, 1372; Neslage, Tr. 8720-23.

[241] CX 1666.

ture and sell, in a specified geographic territory, soft drinks in bottles and cans bearing the concentrate company's trademark and using its formula.[242] This feature is universal for packaged branded CSDs and for pre-mix fountain syrup, and partial for post-mix fountain branded CSDs.[243] We will first address the operation of exclusive territories for sales of packaged branded CSDs and pre-mix fountain syrup.

Under the exclusive franchise agreements, concentrate firms prohibit their franchised bottlers from transshipping, that is, from shipping packaged CSD products, pre-mix fountain syrup, and concentrate outside of the exclusive franchise territory for which they are licensed into the franchise territory of another bottler.[244] The restrictions against transshipping are vigorously enforced.[245] Indeed, they have become stricter over time, with increased penalties and tighter monitoring.[246]

Because territories of the branded CSD bottlers are exclusive, branded CSD bottlers outside of the San Antonio market would be contractually prohibited from selling packaged CSDs to a San Antonio customer that looked for an alternative seller outside the San Antonio market in order to a small but significant, nontransitory price increase by a San Antonio branded CSD bottler. Moreover, the impact of territorial exclusivity within the San Antonio market is highlighted by the fact that the major branded CSD bottlers in San Antonio also possess exclusive rights in various other portions of the immediately surrounding area beyond the ten-county San Antonio market. *See, e.g.*, IDFF paragraph 275-77 (showing CCSW, Pepsi and Grant-Lydick's exclusive franchises in Texas).[247] Consequently,

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[242] *See* CX 102 G; CX 1666 A-E; CX 418 F; CX 1853 ZI; RX 2850 A; Howell, Tr. 4004; Dr Pepper Company, RX 2908 A-D; E. Hoffman, Tr. 381-82; Bodnar, Tr. 1372; Neslage, Tr. 8720; CX 574 A; CX 896 Z6; CX 891 K.

[243] All major concentrate firms provide exclusive geographic territories for their pre-mix fountain syrup. Summers, Tr. 6894 Davis, Tr. 4470; Knowles, Tr. 2671, 2681; CX 379 Z71-Z84; CX 1667 B-C; Strickland, Tr. 8681; Turner, Tr. 1086; CX 1406 Z5. While Pepsico provides exclusive geographic franchise territories for its post-mix fountain syrup (Davis, Tr. 4470; Knowles, Tr. 2670; Strickland, Tr. 8681; Turner, Tr. 1086), CCUSA and Dr Pepper do not (Knowles, Tr. 2681; Summers, Tr. 6895; Strickland, Tr. 8681; Turner, Tr. 1086; Cassagne, Tr. 7619; CX 418 K).

[244] CX 1667 A-D; CX 1853 ZI; Davis, Tr. 4473-74; Knowles, Tr. 2742; Turner, Tr. 1055; Schwerdtfeger, Tr. 2414-15.

[245] CX 1667 A-D; CX 3009 A-B; CX 3432 B; RX 2850 B; CX 3414 A-C, RX 2908 B; Knowles, Tr. 2743-44; CX 3976 at 2111-12 [Quirk]; Summers, Tr. 6901, 6920; CX 2203 A; CX 3011; Schwerdtfeger, Tr. 2414-15.

[246] Davis, Tr. 4473-74; Little, Tr. 674-75, 679.

[247] *See also* RX 352 (CCSW); RX 2973 (Pepsi).

a collective price increase by the branded CSD bottlers in the San Antonio market would be far more difficult to defeat than in conventional markets.

San Antonio retailers uniformly testified that they would not purchase their branded CSD requirements from an outside bottler even if the outside bottler offered substantially lower prices.[248] This is because retail accounts will abide by bottlers' geographic territory limitations, and therefore will not purchase outside of those territories or transship into their own territories, even if CSD prices were to go up significantly.[249] In addition, retailer transshipment is unlikely due to the high cost of DSD delivery.[250] Retailers are presumably also reluctant to purchase transshipped products because the retailers would have to compensate for the loss of DSD marketing assistance,[251] a factor as important as price in the sale of CSDs.[252] We therefore turn next to the possibility of unauthorized transshipments by branded CSD bottlers.

Importantly, the record shows very few, if any, significant instances of transshipment of branded CSDs into the San Antonio

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[248] CX 3963 at 28-29 [Thurmond]; E. Hoffman, Tr. 388-90; Davis, Tr. 4476;Chapman, Tr. 7213; Hiller, Tr. 5367; CX 3815 at 28-29 [Joyner]; CX 3814 at 35 [Adams]; CX 3985 at 89 [Daub]; CX 1853 Zl; Little, Tr. 659-60, 674-76, 679.

[249] *Id.*

Another possible explanation for retailers' unwillingness to purchase outside the San Antonio market if faced with a price increase may be that retailers do not absorb price increases charged by bottlers, but rather typically respond by passing the price increase along to the ultimate consumers. Kaiser, Tr. 3196; Chapman, Tr. 7212, 7255-56; Brinkley, Tr. 2235; Anderson, Tr. 3904; Davis, Tr. 4533; Donald, Tr. 5300-01; Turner, Tr. 991. Because retailers would therefore likely pass on a 10% price increase (Anderson, Tr. 3904; Turner, Tr. 991; Donald, Tr. 5300-01), profitability would be relatively unaffected and retailers would have little motivation to undermine the increase.

[250] DSD delivery, which generally involves delivery to the actual retail outlet, unpacking, and reshelving (Turner, Tr. 955-56, 1530-31, 6414-15), obviously entails high costs. *See* RX 0867 *supra* (study by CCUSA indicated that distribution accounts for about 35% of a bottler's costs). This would be even more true for retailer transshipment, where the retailer would also have to gather previously-delivered bottles and cans and repack the trucks. The record evidence indicating that shipping costs are relatively low (Amrosowicz, Tr. 807, 859-60) refers only to the freight costs incurred in shipping in bulk quantities from warehouse to warehouse.

[251] Bottlers pay for DSD, but retailers must pay for warehouse delivery. Summers, Tr. 6469.

[252] Summers, Tr. 7119.

market by franchised bottlers.[253] Since it therefore appears that only relatively small quantities of branded CSDs have been transshipped into San Antonio, the issue is whether a price increase would induce transshipments in quantities sufficient to undermine that increase. We do not believe that this is a likely occurrence, for a variety of reasons.

First of all, as previously noted, exclusive territories are defined and enforced by concentrate companies, which strictly prohibit transshipping. Substantial penalties are imposed against an offender, creating monetary disincentives against transshipping.[254] Also, the offended bottler is compensated for the loss of sales,[255] thus creating an additional incentive to monitor and enforce prohibitions against transhipping. In fact, CCSW has complained against a bottler for as little as ten cases of transshipped product.[256]

Transshipping is also relatively easy to detect. DSD delivery provides bottlers with day-to-day contact with retail stores, and bottlers can often identify products by means of date codes and proprietary labels.[257]

End-use consumers will not undermine a price increase because it would not be worthwhile for most consumers to drive the substantial distance required to exit the ten-county San Antonio market

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[253] In the initial decision, the ALJ listed the major instances of transhipping shown in the record. *See* IDFF paragraph 288-94. Notably, however, these examples all involved transshipment between areas outside of San Antonio (IDFF paragraph 288-92; *but see* IDFF paragraph 293 (transshipping fines paid for undefined transgressions)) or by retailers (IDFF paragraph 294; RX 3121). None of them involved significant shipments of branded CSDs into San Antonio by franchised bottlers. *See* CX 3645 Z46 (69 cases of Coca-Cola and 20 cases of Dr. Pepper estimated to have been shipped into San Antonio over a two-month period in 1988). Moreover, the evidence of transshipment outside of San Antonio demonstrates that, in general, transshipment is minimal relative to total sales volume. Thus, for example, the fact that CCE paid more than $1 million in transshipment penalties in 1989 (IDFF paragraph 293) pales in comparison to the company's sales of almost $4 billion (Standard and Poor's Register of Corporations 624 (1990)); this penalty represents transshipments of far less than 1% of sales. Similarly, although SWCC received over $200,000 in transshipping penalties in 1986 and 1987 (IDFF paragraph 291), this is less than .2% of SWCC's 1989 net sales. *See* CX 891 Z3; CX 1357 Z3. The 230 complaints against Pepsi COBO, mostly by the Oneta Company (IDFF paragraph 289), are likewise *de minimis* in comparison to Pepsi CODO's annual sales of around 11 million cases (RX 1238) and Oneta's annual sales volume of around $10 million, representing about 1.5 million cases per year (Koch, Tr. 1906-07; CX 4114; RX 3085).

[254] CX 3432 B; CX 531; CX 538; CX 2927; CX 534; CX 539; CX 1667.

An additional disincentive bottlers face is that parent concentrate companies may regulate the amount of concentrate that bottlers obtain in order to prevent them from transshipping. CX 1853 ZI.

[255] Davis, Tr. 4822; E. Hoffman, Tr. 383; CX 379 Z41; CX 2327 A-F.

[256] Summers, Tr. 6903-04; CX 2296 B.

[257] E. Hoffman, Tr. 393-94; CX 3667 E.

simply to purchase CSDs at a slightly lower price. This common-sense conclusion is supported by ample record evidence.[258]

Thus, with respect to the overwhelming majority of branded CSD sales for which exclusive geographic territories exist, we conclude that there is no competitive force that would effectively defeat a small but significant, nontransitory price increase on branded CSDs in the San Antonio market. We next examine whether the existence of non-exclusive geographic territories as to certain post-mix fountain sales requires any different conclusion.

Dr Pepper franchises assign exclusive territories for bottlers' sales of post-mix fountain syrup, but allow food wholesaler and broker sales within a bottler's exclusive territory.[259] Coca-Cola franchises do not grant any exclusive geographic territories for post-mix fountain sales.[260] In addition, as noted earlier, both CCUSA and DPUSA control national account pricing for branded CSDs.[261] Thus, for post-mix fountain sales of Coke and Dr Pepper products from outside a San Antonio market, customers may look to Coke bottlers outside of San Antonio, food wholesalers and brokers, and the parent concentrate companies. Other branded concentrate companies assign exclusive territories for post-mix fountain syrup sales.[262]

These somewhat different facts do not lead us to any different geographic market definition, however. The Coke bottlers around San Antonio are CCSW itself and its sister corporation, SWCC; SWCC would be unlikely to constrain a price increase by CCSW.[263] Food wholesalers and brokers must obtain fountain syrup from some

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258 The San Antonio market is a compact population center surrounded by large, sparsely populated areas. *See* CX 1684 C; *see also* CX 4131, CX 4149. Indeed, a single county in this market, Bexar, contains approximately 86% of the total ten-county population. *See* CX 4131 A. This population distribution suggests limited alternatives for San Antonio consumers beyond the immediate market. Also, national and regional retailers view San Antonio as a separate retail market (*see* CX 3963 at 10-11 [Thurmond]; Hiller, Tr. 5332, 5347; CX 3985 at 8-9 [Daub]), thus demonstrating that consumers tend to shop in this area, and not beyond.

259 Turner, Tr. 1086-87; Short, Tr. 7597, 7619-20.

260 Knowles, Tr. 2681; Summers, Tr. 6895.

261 *See* note 68 *supra*.

262 This includes sales of post-mix fountain of Pepsi, RC, and 7-Up, all of which grant exclusive geographic territories as to post-mix fountain syrup. Davis, Tr. 4470; Knowles, Tr. 2670, 2681-82; Turner, Tr. 1086.

263 Both corporations are controlled by TBG. *See* Section II *supra*. CCSW's current franchise territory includes San Antonio and sixty counties in southern, central, and eastern Texas. IDFF paragraph 275. SWCC is the Coca-Cola bottler in west Texas. *See* Section II *supra*.

source; in the face of a hypothetical collusive price increase by input suppliers in the San Antonio market, food wholesalers and brokers, as a practical matter, would have to rely on the same sources we have outlined above: bottlers with exclusive rights in other portions of the immediately surrounding area and national concentrate companies that also sold inputs in the immediately surrounding area.[264]

We therefore conclude that, for the entire branded CSD product market, there is no competitive force that would effectively defeat a small, but significant and nontransitory price increase in the San Antonio market. Thus, we disagree with the ALJ's assessment of the relevant geographic market issue.

Rather than attempting to ascertain whether branded CSD bottlers in the San Antonio market could collusively impose a small but nontransitory price increase, the ALJ instead relied primarily, and almost exclusively, on the Elzinga-Hogarty test of shipping patterns.[265] *See* ID 64-65. However, the Commission has previously found no basis for "definitive reliance" on the Elzinga-Hogarty test to establish a geographic market under the Clayton Act. Adventist Health System, 5 Trade Reg. Rep. (CCH) paragraph 23,591 at 23,259. Consequently, the Commission "does not . . . endorse either the 'strong' or the 'weak' test as the basis for establishing a relevant market." *Id.* at 23,260.

Shipping patterns, whether analyzed using the Elzinga-Hogarty methodology or in some other fashion, clearly constitute one source of information in analyzing the possible exercise of market power. But other evidence is equally relevant. Adventist Health System, 5 Trade Reg. Rep. (CCH) paragraph 23,591 at 23,259. In other words, shipping patterns are only one of many surrogates for assessing market power (*see, e.g., B.F. Goodrich Co.*, 110 FTC at 289), and

[264] Although in theory food wholesalers and brokers might purchase fountain syrup from far outside the San Antonio area and ship it into San Antonio, the record is silent on whether it would be cost effective for wholesalers or brokers to do so in the face of a 5% or similar price increase on fountain syrup.

We are not implying that national concentrate companies would necessarily participate in any collusive branded CSD price increase; that is an issue we will address later. *See* Section VI.C *infra*. Rather, we are simply assessing the alternatives available to customers in the face of a hypothetical collusive price increase in post-mix fountain syrup. If the national concentrate companies participated in such a price increase, then it would be highly unlikely that they would undermine their own price increase in San Antonio by permitting food wholesalers and brokers to obtain fountain syrup at a lower price outside San Antonio.

[265] *See* Kenneth Elzinga & Thomas Hogarty, The Problem of Geographic Market Delineation Revisited: the Case of Coal, 23 Antitrust Bull. 1 (1978); Kenneth Elzinga & Thomas Hogarty, The Problem of Geographic Market Delineation in Antitrust Suits, 18 Antitrust Bull. 45 (1973).

therefore should not be overemphasized, as the ALJ erroneously did here in describing them as "perhaps the best test in determining a geographic market." ID 64.

Moreover, the Elzinga-Hogarty test is less relevant to settings like this one, where territorial exclusivity imposes legal and contractual impediments to transshipping by competitors.[266] By virtue of exclusive territories, legal bottler shipments from outside the geographic area (*e.g.*, contract packing) are controlled by franchised bottlers within the area;[267] other shipments are in violation of contract. Shipments from outside the San Antonio market that are under the control of a hypothetical collusive group would obviously not be used to defeat a price increase. Because the Elzinga-Hogarty test nonetheless takes such shipments into account, the test is an especially imperfect measure of market power in this case. Finally, to the extent that the Elzinga-Hogarty test has some limited value in the present context, the ALJ completely undermined the test by using the wrong product market, thus skewing the analysis.[268]

Relative prices and movements of those relative prices are additional surrogates for the ability to exercise market power and, as such, can be useful considerations to assist in defining a geographic market. *See B.F. Goodrich Co.*, 110 FTC at 289. If prices of branded CSDs in the San Antonio area moved together with one another, and independently from prices in other areas, this would support the conclusion that there is a San Antonio market.

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[266] Hilke, Tr. 6240-41.

[267] CCSW produces cans in its Cuero facility outside the San Antonio market for distribution in San Antonio and elsewhere throughout its franchise territory. Summers, Tr. 6403-04. Grant-Lydick purchases its products from contract packers outside the San Antonio market. Turner, Tr. 929, 1117; Bodnar, Tr. 152627, 1557; Campbell, Tr. 1926, 1987; Espinoza, Tr. 4248-49. Pepsi COBO also imports both bottles and cans from outside the San Antonio market. Davis, Tr. 4461-62, 4464, 4630-32.

[268] If all shipments of branded CSDs into and out of the San Antonio market that were not controlled by the franchised San Antonio bottlers were taken into account, the LIFO calculations would range from 78% to 85%, indicating a market. *See* CX 4089. (If analyzed in this manner, we would consider LOFI calculations irrelevant to the question of whether a price increase could be constrained in the present case.) Moreover, if an ElzingaHogarty analysis were conducted to measure shipments of take-home branded CSDs into and out of the San Antonio market that were not controlled by the franchised San Antonio bottlers both the LIFO ("little in from outside") and LOFI ("little out from inside") figures would approach 100%, thus satisfying even the most stringent Elzinga-Hogarty test. RX 3062 A.

In reaching this conclusion, we reject respondent's assertion that this is a "tautological" approach that "assum[es] away the data of any supplier whom [the Commission] might choose to include in the market." ABR-A 43. We simply believe it is inappropriate to reduce the LIFO and LOFI numbers by including shipments into or out of San Antonio that are controlled by the franchised San Antonio bottlers, because such shipments clearly would not be used to defeat a price increase.

While the only systematic price data in the record show differences in percentage price changes between the areas of San Antonio, Waco, and Corpus Christi,[269] there is also at least some weak evidence suggesting price uniformity throughout at least some bottling territories.[270] On balance, we find the evidence on relative prices and price movements to be weakly supportive of complaint counsel, but relatively unreliable, and therefore we do not rely on it.[271] We do not view the essentially inconclusive nature of this evidence as significant, however, because the more probative evidence strongly points to the existence of a San Antonio market, and also because the confounding effects of ad features and in-store displays would, in any event, limit our ability to discern true price variations.[272]

Finally, it is clear from the record that recognition of a San Antonio market comports with both economic and geographic realities. From an economic perspective, a number of trade and marketing factors support this market definition. For example, national and regional retailers view San Antonio as a separate retail market.[273] These retailers run localized advertising and marketing campaigns that treat the San Antonio market as a separate and distinct marketing area.[274] Retail prices and sales of CSDs in the San Antonio market are compiled separately, and compared to prices and sales in other geographic markets.[275] The behavior of retailers thus constitutes strong confirmation of the existence of a San Antonio market.

Viewed from a geographic and demographic perspective, a San Antonio market is eminently sensible. The San Antonio area is a

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269 *See, e.g.*, CX 3999 A, E.

270 *See, e.g.*, Summers, Tr. 6711, 6719; RX 2985.

271 In reaching this conclusion, we reject the ALJ's essentially unsupported finding that CSD prices "are uniform in a trade area beyond the ten-county area." ID 66. Although the ALJ found that H.E.B. preferred a uniform price throughout its territory, the cited testimony demonstrates that local competitive conditions generally prevented this (Chapman, Tr. 7247, 7200-01). The exhibit (RX 2985) cited for the proposition that numerous bottlers (Pepsi COBO, CCSW, CCE and Grant-Lydick) offered H.E.B. uniform pricing applies only to Pepsi COBO, not to the other companies, and fails to reflect the fact that those prices were often not accepted. *See* CX 4111; Hilke, Tr. 8507-08.

272 Another problem with price movement data is that prices change seasonally, so that prices of different brands and products will reflect this seasonality whether they are in the same market or not. This means any simple "statistical analysis" of sign changes can be misleading, and is yet another reason why we believe that comparisons of price movements are of little value here.

273 Hiller, Tr. 5333, 5347; CX 580; CX 3963 at 10-11 [Thurmond].

274 Chapman, Tr. 7198-200; Kaiser, Tr. 3187-89; Hiller, Tr. 5347; CX 1054 P-S.

275 CX 2263 F-R, U-Z6; CX 580; Kaiser, Tr. 3188-89; CX 1014 A-M.

compact population center, with 86% of its population in a single county, that is surrounded by large, sparsely populated areas.[276] By virtue of this population distribution, consumers in the San Antonio market would appear to have only limited realistic alternatives beyond the immediate market.

In sum, we conclude that the ten-county San Antonio market is the relevant geographic market within which to assess the challenged acquisition.

VI. THE LIKELY COMPETITIVE EFFECTS OF THE ACQUISITION

The purpose of Section 7 of the Clayton Act is to prevent mergers or acquisitions whose effect "may be substantially to lessen competition, or to tend to create a monopoly."[277] To fulfill this purpose, we seek to discern whether a particular transaction is likely to create or enhance market power or to facilitate its exercise.[278]

"Market power" is "the ability profitably to maintain prices above competitive levels for a significant period of time," or to "lessen competition on dimensions other than price, such as product quality, service, or innovation."[279] In certain circumstances, firms may exercise market power jointly through collusive conduct. Thus, one prong of our inquiry focuses on whether the transaction under scrutiny here may enable the acquiring firm to cooperate (or cooperate better) with other leading competitors in raising price or reducing output or colluding on other aspects of competition.[280] In other circumstances, a firm may exercise market power unilaterally by raising price and reducing output.[281] Thus, the other prong of our inquiry focuses on whether the acquisition at issue here may facilitate the exercise of unilateral market power.

The ALJ found that, since complaint counsel had failed to establish a relevant product market, an accurate measure of concentration

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[276] *See* note 258 *supra*.

[277] 15 U.S.C. 8. Mergers are subject to Section 5 of the Federal Trade Commission Act if they constitute an "unfair method of competition."

[278] Merger Guidelines, Section 0.1.

[279] Merger Guidelines, Section 0.1 & n. 6; Owens-Illinois, slip op. at 4-5 (quoting 1984 Guidelines).

[280] *See HCA v. FTC*, 807 F.2d at 1386; *B.F. Goodrich*, 110 FTC at 294.

[281] Merger Guidelines, Section 2.2.

levels was not possible, and that, in any case, there was a "wealth of proof of competition" in CCSW's trade. ID 67. As set forth above, we find that the ALJ erred in his assessment of the relevant product and geographic market. Using the correct relevant market -- branded CSDs in San Antonio and the immediately surrounding counties -- we find that there is ample evidence of the likelihood of competitive harm from the acquisition at issue here, both in terms of likely coordinated interaction and unilateral effects.

A. Market Concentration

In *United States v. Philadelphia National Bank,*[282] the Supreme Court noted that a crucial initial question in merger cases is whether the transaction at issue "produces a firm controlling an undue percentage share of the relevant market, and results in a significant increase in the concentration of firms in that market, [such that] it is..... inherently likely to lessen competition substantially...." 374 U.S. at 363; *accord, B.F.Goodrich,* 110 FTC at 303-304.

The transaction at issue in this case raised concentration levels significantly in an already highly concentrated market, as measured by the Herfindahl-Hirschmann Index ("HHI").[283] The following are the pre- and post-acquisition HHIs in the relevant market:

Pre-acquisition HHI	2807
Post-acquisition	3421
HHI Increase	614[284]

Under the Merger Guidelines, "[w]here the post-merger HHI exceeds 1800, it will be presumed that mergers producing an increase in the

[282] 372 U.S. 321 (1963).

[283] The HHI is calculated by summing the squares of the market shares of the market participants. The HHI ranges from 10,000 in a pure monopoly to near zero in a purely atomistic market. Merger Guidelines, Section 1.5 & n. 17.

[284] CX 4146A, H. These data were provided by complaint counsel, but they are based on data used by respondent's expert, Dr. Strickland, in RX 3057 and RX 3058, with adjustments made to equate fountain units with package units. We rely on these data, rather than complaint counsel's proposed HHI calculations because these data include CCUSA, DPUSA, and fountain wholesalers in the market as sellers of post-mix fountain syrup. We agree with respondent that those post-mix fountain sales must be attributed to the entity that sets the price for the sales, not to CCSW, although CCSW does deliver many of these sales for a delivery fee from the parent concentrate company. *See* Summers, Tr. 6500-6501, 6507.

HHI of more than 100 points are likely to create or enhance market power or facilitate its exercise." Merger Guidelines, Section 1.51. These figures show that the relevant market was highly concentrated before the acquisition and became significantly more so as a result of the acquisition.

The resulting post-acquisition HHIs are in the same range as or higher than those in most of the cases in which the Commission has successfully litigated a challenge to a merger or acquisition in the last ten years.[285] For example, they significantly exceed the HHIs in the VCM market in B.F. Goodrich, which were found to justify a "relatively strong presumption of anticompetitive effects."[286] These HHIs, which are much larger, create a strong presumption of possible anticompetitive effects; thus, relatively strong evidence from other factors will be necessary to rebut that presumption.[287]

B. The Significance of Increased Concentration

The ALJ and respondent assert that these HHIs do not carry the same significance as other HHIs because, although they show a large increase in concentration, the number of market participants has remained the same. This argument ignores certain aspects of the information conveyed by HHIs, information that is particularly crucial to an accurate understanding of competition and the likeli-

[285] *See* Coca-Cola, slip op. at 44 (HHI increase of 443 to post-merger HHI of 3572); Occidental Petroleum Corp., Dkt. No. 9205 (Dec. 22, 1992), slip op. at 27 (post-acquisition HHI in one market of 1305 with increase of 158 points); Owens-Illinois, slip op. at 27 (using production figures, post-acquisition HHI of 2478 with increase of 852 points); *Olin Corp.*, 113 FTC 400, 610-11 (1990), *aff'd*, 986 F.2d 1295 (9th Cir. 1993), *cert. denied*, 114 S. Ct. 1051 (1994) (based on production, post-acquisition HHI of 4122, with increase of 1186); *Hosipital Corp. of America*, 106 FTC 361, 488 (1985) (post-acquisition HHI of 2416 with increase of 395 points).

[286] In B.F. Goodrich, the parties presented various measures of the HHIs in the VCM market (*e.g.*, nameplate capacity, practical production capacity, and actual production). The highest HHI figures were those for actual production, which showed an HHI increase of 304 to produce a post-acquisition HHI of 1663. *B.F. Goodrich*, 110 FTC at 313. The Commission found that the data were "well above those that created a presumption of illegality in *United States v. General Dynamics* and *Weverhauser*," and that the data supported a "relatively strong presumption of anticompetitive effects." 110 FTC at 314.

[287] *See PPG*, 798 F.2d at 1502-03 (acquisition resulting in 1352 point increase in HHI to post-acquisition HHI of 3295 put merger "well within the range where, absent really extraordinary circumstances, the Department and the Commission will proceed against an acquisition under section 7 of the Clayton Act on the theory that the increased concentration raises a likelihood of 'interdependent anticompetitive conduct'" [citations omitted]); *B.F. Goodrich*, 110 FTC at 314.

hood of collusion among and/or unilateral anticompetitive conduct by branded CSD bottlers.[288]

The HHI conveys information about both the number of market participants and the size disparity of the market shares among market participants. As explained by then-Judge Bork, writing for the Court of Appeals for the District of Columbia Circuit in *FTC v. PPG Industries, Inc.*:

> Market power or the lack of it is often measured by the HHI. The FTC and the Department of Justice, as well as most economists, consider the measure superior to such cruder measures as the four- or eight-firm concentration ratios which merely sum up the market shares of the four or eight largest firms. The HHI, by contrast, is calculated by squaring the individual market shares of all firms in the market and adding up the squares. This method, unlike the four- and eight-firm concentration ratios, shows higher market power as the disparity in size between firms increases and as the number of firms outside the first four or eight decreases.

PPG, 798 F.2d at 1503 (emphasis added). Market share, of course, is an initial proxy for market power, since we typically have no direct means by which to measure market power. One premise underlying antitrust jurisprudence is that, absent other factors, a firm's market power is likely to increase as its market share increases, and that its market power relative to other market participants increases as its share becomes disproportionately larger than the shares of other market participants.[289]

In this case, the three main soft drink bottlers in the relevant market stayed the same -- CCSW, Pepsi COBO, and Big Red Bottling (now owned by Grant-Lydick) -- and the other sellers of post-mix fountain syrup (CCUSA, DPUSA, and fountain wholesalers) also remained the same. However, the acquisition increased CCSW's pre-acquisition market share from 44.7% to 54.5%.[290]

We conclude, based on the record, that CCSW's acquisition of the Canada Dry franchise, which accounted for only about 1% of this market share increase, had no anticompetitive effect. If only the

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[288] As we discuss in Section VI.C.1 *infra*, we do not find that tacit collusion among the branded CSD bottlers in the relevant market would likely be prevented or disrupted by the other market participants that sell post-mix fountain syrup that is, the parent concentrate companies and food wholesalers and brokers.

[289] *See Warner Lambert Co.*, 87 FTC 812, 870 (1976); *see also Heublein, Inc.*, 96 FTC 385, 577 n. 10 (1980); W. Shepherd, Market Power and Economic Welfare 40 (1970).

[290] CX 4146 H.

Canada Dry franchise had been transferred to CCSW, the pre- and post-acquisition HHIs would be as follows:

Pre-acquisition HHI	2807
Post-acquisition HHI	2862
HHI Increase	55

See CX 4146 H; CX 4079. Under the Merger Guidelines, such a change would be viewed as "potentially rais[ing] significant competitive concerns . . . ." Merger Guidelines Section 1.51. In terms of the competitive issues we discuss next, however, we find that virtually no evidence exists to demonstrate that a one-percent increase in CCSW's market share due to an acquisition of the Canada Dry franchise would provide CCSW with significantly greater market power than it already had and thus would substantially lessen competition. We note that a one percent -- or even less -- market share increase might have competitive significance in circumstances where the one percent was being combined with several other low-percentage shares. In this transaction, however, it is clear that the 8.6% market share increase from the Dr Pepper franchise acquisition is the true source of the likely anticompetitive effects that we describe in the following sections.

The acquisition of the Dr Pepper franchise increased CCSW's market share by about 8.6%.[291] This acquisition changed the number of product offerings that each firm had available and thus changed CCSW's and Big Red Bottling's relative costs of and advantages with respect to producing and marketing their branded CSDs.

As we explain in more detail below, such changes can significantly affect the ability and incentive of smaller bottlers such as Big Red Bottling to compete. In this case, the evidence confirms that CCSW's acquisition of the Dr Pepper franchise provided CCSW with increased market power and left Big Red Bottling facing significant disadvantages.[292] As we discuss further below, this situation increases both the likelihood that CCSW and the Pepsi COBO could tacitly and successfully collude with Big Red Bottling -- since Big Red Bottling would have little or no ability or incentive to do any-

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[291] *See* CX 4146 H; CX 4079 B; CX 1681 C.

[292] *See* Section VI.C.2 *infra*.

thing other than follow -- and the potential for an exercise of unilateral market power by CCSW.

C. The Likelihood Of Successful Collusion

1. The Market Participants Required for Successful Tacit Collusion

The first issue to be addressed is whether the presence of CCUSA, DPUSA, and fountain wholesalers as sellers of post-mix fountain syrup could prevent or disrupt any tacit or explicit collusive arrangement among the bottlers of branded CSDs in the San Antonio market. We find that fountain wholesalers would be unlikely to disrupt a hypothetical collusive arrangement that included bottlers and the parent concentrate companies, because fountain wholesalers must obtain fountain syrup either from bottlers or from the parent concentrate companies. Thus, the key issue is whether CCUSA and DPUSA might be likely to participate in a collusive arrangement with bottlers as to San Antonio sales of branded CSDs, including post-mix fountain syrup.

The evidence indicates that it is highly unlikely that either CCUSA or DPUSA would have the incentive to become part of a collusive arrangement in the San Antonio area. Both CCUSA and DPUSA use "national account" pricing for their post-mix fountain sales -- that is, pricing that is uniform across the geographic areas in which the chains and other purchasers of post-mix fountain syrup operate.[293] CCUSA representative Short testified that this is one of the advantages perceived by the chain customers.[294] Thus, there does not appear to be any incentive for either CCUSA or DPUSA to deviate from their national account pricing solely in the San Antonio area. Moreover, such a deviation would be highly noticeable and presumably hard to justify.

This does not mean that CCUSA and DPUSA post-mix fountain syrup sales would necessarily be sufficient to constrain an overall collusive branded CSD price increase instituted by the bottlers, however. First, as to post-mix fountain sales, both the CCUSA and the DPUSA representatives testified that they did not compete with

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[293] Short, Tr. 7739, 7797; Knowles, Tr. 2820.

[294] Short, Tr. 7797.

the bottlers for the accounts to which the bottlers sold post-mix fountain syrup, because the bottlers typically served smaller accounts than those served by CCUSA or DPUSA.[295] Thus, there is some reason to doubt that CCUSA or DPUSA would respond aggressively to a collusive branded CSD price increase by bottlers. Second, because post-mix fountain products (the channel in which CCUSA and DPUSA are present) are differentiated from other branded CSD products, it does not appear that expanded sales of post-mix fountain syrup by CCUSA and DPUSA would be sufficient to constrain a collusive overall branded CSD price increase by bottlers. Therefore, we turn next to whether CCSW's acquisition of the Dr Pepper franchise increased the likelihood of tacit collusion by branded CSD bottlers in San Antonio.

2. The Increased Likelihood of Tacit Collusion in the Take-Home Channel: Ad Features

The record suggests that CCSW's acquisition of the Dr Pepper franchise may have had an effect on Big Red Bottling's ability to obtain ad features, a significant element of competition. As we explained earlier, the most significant discounting and volume generation for take-home sales of branded CSDs occurs through ad features.[296] The loss of significant franchises could reduce the ability of the smaller bottler to obtain ad features in retail chains, a key component in effective competition among branded CSDs. Without ad features, price decreases have much less effect on attracting volume.[297] Moreover, even if the smaller bottler were still able to

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[295] CCUSA will provide national account pricing to any qualified entity with five outlets; DPUSA will provide national account pricing to any qualified entity with three outlets. Short, Tr. 7735-36; Knowles, Tr. 2821. Mr. Short of CCUSA testified:

Q. So then are you in competition with Coke Southwest for fountain accounts?

A. Not for fountain accounts, no. Not to pick up a fountain account. I have a segment of the business that I -- We manage the whole business. We allow them to go manage the local side of the business, and that's the part they manage. But we don't compete for that business.

Q. Does Coke Southwest compete for your national accounts?

A. No.

Short, Tr. 7800-01. Mr. Knowles of DPUSA testified that, for fountain sales not covered by DPUSA's national account price, "[t]hat's basically the bottler selling up and down the street to the buy downstairs, and he doesn't have a contract. So, I mean, who knows what he's paying for his syrup." Knowles, Tr. 2820. Indeed, Mr. Knowles testified that the prices at which bottlers sold post-mix fountain syrup probably already ran higher than DPUSA's national account price, but that he didn't know because "[w]e just don't get into it." Knowles, Tr. 2824.

[296] *See* Section IV.C.3 *supra*.

[297] *See id*

obtain some ad features, the loss of significant franchises might mean that those ad features would cost the smaller bottler significantly more than was previously the case -- another deterrent to effective competition. In addition, smaller retail outlets with limited shelf space are more likely to carry the high volume brands, other things being equal.[298]

Conversely, the addition of significant franchises to the holdings of a larger bottler such as CCSW could increase its advantages in terms of ad features. As a result, the smaller bottler may become less willing to challenge the market strength of the larger bottler through vigorous price competition and more willing to become a follower of noncompetitive market activity. We next examine whether the evidence demonstrates an increased advantage for CCSW and a decreased ability by Big Red Bottling to obtain ad features.

a. Big Red Bottling's Loss of "Critical Mass"

Ad features involve significant retailer advertising of specially discounted products. Retailers use ad features offering sharply discounted branded CSD prices as a means to "pull" customers into their stores. For example, Kaiser representative Mr. Kroger testified that: "We consider soft drinks the best customer count produced of any feature we run. It is the best item in grocery to run as a feature."[299] Thus, branded CSDs are used by retailers as volume generators and to increase consumer foot traffic.[300] They are often sold at cost or even as loss leaders in order to generate retail store volume.[301] As with retailers nationally, San Antonio retailers recognize CSDs as one of the largest, if not the largest, retail food item and promote them accordingly.[302]

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298 *See id.*

299 Kaiser, Tr. 3231-33.

300 Davis, Tr. 4709; Turner, Tr. 1206; CX 3815 at 153 [Joyner]; Anderson,, Tr. 3840-41, 3896; Chapman, Tr. 7256; Clarke, Tr. 4280; Brinkley, Tr. 2188; Knowles, Tr. 2840; CX 3821 at 48 [Imper]; CX 3814 at 54 [Adams].

301 Kaiser, Tr. 3185-86; Coyne, Tr. 3485-86; Chapman, Tr. 7256; Turner, Tr. 973-74, 1206-07; Anderson, Tr. 3840-41; Clarke, Tr. 4280; Donald, Tr. 5289, 5297-98; Gonzaba, Tr. 2085; Brinkley, Tr. 2188; Sendelbach, Tr. 7696; Bodnar, Tr. 1570. These low prices are often known as "hot prices." Howell, Tr. 3952. *See also* IDFF paragraph 425 ("H.E.B. uses soft drinks as a loss leader").

302 Sendelbach, Tr. 7695; Donald, Tr. 5288; Brinkley, Tr. 2187. San Antonio retailers advertise and promote branded CSDS, often at prices which are at or below cost. Sendelbach, Tr. 7698; Anderson, Tr. 3841; Turner, Tr. 973-74.

For branded CSD bottlers, the first priority for promotions is to get into the ad cycle. The second priority would be to have in-store displays.[303] A bottler cannot grow its brands without attaining the volume lift benefit associated with an ad feature in the ad cycle; in-store specials alone are not enough to obtain the necessary volume increases.[304] As discussed in Section IV, *supra*, bottlers are aware that ad features give much more volume "lift" than do in-store displays.[305]

Without "critical mass" or market share, however, a bottler's ability to get into the ad cycle is reduced because the retailer will not give a week of its ad cycle to a product that will not attract significant numbers of customers.[306] "Critical mass" as related to advertising means that a bottler has a significant enough market share and consumer appeal that retailers believe it draws customers into the store.[307] The more products or flavors a bottler has in its stable of products, the greater the overall ability it has to sell product.[308] If a bottler only has a single brand, it requires significant brand equity or recognition to sell products.[309] In order to put a CSD in an ad cycle, the retailer must be convinced that the CSD would be a good customer draw.[310] The bottler must have the market share or "pull-through" necessary to obtain the critical mass necessary to get into

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303 E. Hoffman, Tr. 366.

304 Turner, Tr. 974.

305 Bodnar, Tr. 1498; Turner, Tr. 974; E. Hoffman, Tr. 362. An ad feature may give a bottler 10 times the non-featured sales volume, Bodnar, Tr. 1498; Davis, Tr. 4504; Koch, Tr. 1831 while an in-store display gives just twice to 2 1/2 times the normal sales volume, Bodnar, Tr. 1498. A month long display at an attractive price produces close to the same volume as a one week ad, Bodnar, Tr. 1498. The volume lift is much lower on the instore display because the retail price to the consumer is usually higher. Turner, Tr. 974; E. Hoffman, Tr. 362-63. *See also* Section IV.C.3 *supra*.

306 Turner, Tr. 1040-44; CX 3941 at 287 [Schmid].

307 Turner, Tr. 1040

308 CX 3989 at 37 [Shanks].

309 CX 3989 at 37 [Shanks].

For example, Mr. Kaiser of Kroger testified that he would probably not run Dr Pepper on its own as an ad feature because "[i]t would be too weak on its own to offset a Pepsi and/or a Coke feature." Kaiser, Tr. 3232-33. Although Dr Pepper has received a few exclusive ads from some of Kroger's competitors, RX 438, even Dr Pepper's own study advised that it should be advertised with Coke to build sales. RX 2825 C.

310 Gonzaba, Tr. 2053. Feature support is very expensive unless there is enough volume to justify it. Coyne, Tr. 3480; CX 971.

the promotional rotation.[311] A bottler is "locked-out" when it receives no promotional period during a particular calendar span.[312]

The testimony of Mr. Kaiser of Kroger is illustrative:

Q. Now in selecting a particular brand to be in an ad-buy program, how important is the customer draw of the product that's being put into the ad?
A. The most important consideration we have is how strong the brand is and how many cases we can sell of it.[313]

The evidence in this case shows that, after Big Red Bottling lost the Dr Pepper franchise, the Big Red bottler became significantly less able to obtain ad features at major supermarkets than it was before the acquisition. Mr. Bodnar, former General Manager of DPSA and currently Executive Vice President, General Manager, and owner of Grant-Lydick, explained that, pre-acquisition, the Big Red bottler had just acquired "critical mass":

A. You know, you have to have the necessary market share or pull-through of the products you represent to have the critical mass, if you will, to get into a promotional rotation, to get the shelf space that you need or the promotional efforts behind the brands that you represent.
Q. At what point . . . did you acquire critical mass . . .
A. I'm going to say in 1983 we started to acquire it with the addition of RC Cola and the fact that we had a cola to offer. . . . Come mid-1983 we started to get feature ads from the major chain supermarkets on a regular basis, again, because of the lineup of brands . . . . would say we more than tripled our ad rate.

Bodnar, Tr. 1254-55. *See also* Turner, Tr. 1043. This situation changed drastically after the Dr Pepper franchise went to CCSW, however.

Q. On average how many ads did you get during the course of the year pre [sic]?
A. With the major chains -- and by that I mean H.E.B., Kroger's, Handy Andy, Albertsons, and Warehouse Grocery -- we were averaging a minimum of one chain per month.
Q. And then after?
A. Never got a Kroger or an Albertsons ad. . . . We did have an ad with Kroger's in part of the stores. . . . So half of an ad. . . . Handy Andy, the first year I

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[311] Bodnar, Tr. 1254. It takes less critical mass to obtain in-store displays. Turner, Tr. 1043.

[312] Davis, Tr. 4740.

[313] Kaiser, Tr. 3231-32.

> would say we continued to get one a month. Warehouse Grocery, one a month. And H.E.B., maybe three ads for the year.

Bodnar, Tr. 1308-09. CCSW's own document confirms Mr. Bodnar's recollections.[314] Indeed, CCSW has conceded that "[i]n recent years, CCSW and Pepsi COBO have used their CMA programs to obtain the majority of ad features offered by San Antonio area retailers." RPFF paragraph 595. Mr. Bodnar testified that Big Red Bottling tried to interest San Antonio retailers in CMAs but was unsuccessful, because Big Red Bottling lacked the necessary volume throughput.[315] That Big Red Bottling has been able to obtain some ad features does not negate the fact that the large majority of ad features have gone to Coke or Pepsi in the San Antonio area.[316]

b. Big Red Bottling's Increased Costs

Dr. Hilke testified that there are economies of scale associated with several aspects of the branded CSD bottling industry and that

[314] CX 2954 H lists the number of feature ads in various San Antonio retailers for 1984 and 1985 for five branded CSDs: Coke, Pepsi, Dr Pepper, 7Up, and Big Red. As Mr. Bodnar recalled, it indicates that Big Red continued to receive about one ad per month from Handy Andy, but that the number of ads from other major chains such as Albertsons and H.E.B. had sharply declined from 1984 to 1985. The precise amount of the decline is difficult to discern, because it is not possible to know how many of the Dr Pepper feature ads took place while the franchise was still held by the same entity as Big Red (DPSA), prior to the August 1984 acquisition of the Dr Pepper franchise by CCSW. However, one can compare the 1984 and 1985 totals with Dr Pepper as part of CCSW and, hypothetically, if it had remained as one of the franchises held by the Big Red bottling operation. According to CX 2954 H, Big Red and Dr Pepper combined throughout all of 1984 would have had 57 feature ads; by contrast, Big Red alone in 1984 would have had only 6 feature ads. For 1985, Dr Pepper and Big Red combined actually would have had 80 feature ads; Big Red alone actually had only 43 feature ads. CCSW alone had 211 feature ads in each of 1984 and 1985; Pepsi alone had 62 feature ads in 1984 and 123 in 1985. Even these comparisons do not show the full extent of the decline for Big Red, but a look at the stores at which Big Red continued to obtain feature ads shows that they are the smaller retailers, not the larger ones like H.E.B.

[315] Bodnar, Tr. 1383-84.

[316] CX 2954 B indicates that, in 1985, for chain supermarkets, Big Red obtained promotions accounting for about 5.3% of all commodities volume, as compared to Coke's 46.9% and Pepsi's 20.9%. For the number of store weeks of ads in major independents, Big Red's share was somewhat higher -- 8.9%, as compared to Coke's 54.6% and Pepsi's 18.6%. However, for share of convenience store ad months, Big Red was practically shut out as was Pepsi -- 5.7% (Big Red) and 5.9% (Pepsi) as compared to Coke's 85.6%. For drugstores and mass merchandisers, Big Red had a 9.6% share of store weeks, compared with Coke's 49.4% and Pepsi's 41.1%. CX 3248 A-E shows that Big Red was able to obtain about 15-20% of promotional activity in the summer of 1985. RX 1678 lists some small independents that gave ad features to Big Red in 1988. A 1989 CCUSA survey found that, for total supermarket displays (not just ad features) in San Antonio, Big Red accounted for 13.6% of the total displays, compared to Coke's 55.4% and Pepsi's 26.6%; the document shows Big Red as totally shut out of convenience store displays. RX 256 B, C. Mr. Bodnar testified that Stop-N-Go ran only Coke features in 1987 and 1988, as did other convenience stores. Bodnar, Tr. 1381.

these economies of scale seem to have increased over time.[317] These economies of scale have been quantified in a study sponsored by the National Soft Drink Association ("NSDA") and executed by the Boston Consulting Group ("BCG").[318] The NSDA report indicates that economies of scale are present in at least three major aspects of bottler manufacturing operations: direct labor, equipment, and materials costs.[319] According to the NSDA study, decreasing bottling output from 4 million cases to 2 million cases, for example, would, on average, entail an increase in the total of these costs from roughly $2.40 to $2.60 per case.[320] This represents an increase of about 8%.[321] In addition, as respondent admitted[322], the per case distribution costs for a bottler generally decrease as the volume or market share of the bottler increases.[323]

The acquisition in this case resulted in the transfer of approximately 42% of DP-SA volume to CCSW prior to the sale of the remaining franchises and assets to Grant-Lydick.[324] Mr. Bodnar noted that it was not until 1989 that Grant-Lydick Beverage Company matched DP-SA's pre-acquisition sales volume level. This did not occur until after Grant-Lydick acquired a number of additional brands, including 7-Up, Dad's Root Beer, Squirt, and Yoo Hoo Chocolate and five more sales locations in 40 additional counties.[325]

In a March, 1987 letter to the Federal Trade Commission, Grant-Lydick Beverage Company supplied pre- and post-acquisition revenue and costs estimates on a per case basis.[326] Grant-Lydick estimated that its average total cost per case increased from $6.37 per case in 1984 to $6.90 in 1985.[327] Grant-Lydick further estimated that

[317] Hilke, Tr. 6054-58, 6042-43; CX 1671; CX 1696.

[318] Hilke, Tr. 6102-05; CX 1697.

[319] CX 1697 I-L

[320] CX 1697 K.

[321] CX 1697 K.

[322] RRCCPFF paragraph 1465.

[323] CX 3941 at 288 [Schmid]. *See also* RX 0867 (CCUSA study indicated that distribution typically accounts for about 35% of a bottler's overall costs).

[324] CX 4079.

[325] Bodnar, Tr. 1347; CX 3830.

[326] CX 1697 E-G.

[327] CX 1697 F.

its production labor cost per case increased from $.12 in 1984 to $.21 in 1985 and that its production overhead cost per case increased from $.37 in 1984 to $.45 in 1985.[328] CCSW disputed these figures, claiming that Grant-Lydick did not sustain any substantial increase in total cost as a result of losing the Dr Pepper and Canada Dry franchises.[329]

However, even CCSW conceded that Grant-Lydick's operating costs increased 7.9% from 1983 to 1986, largely as a result of increased "promotional variable cost."[330] Although respondent characterizes the increased costs of promotion as resulting from increased bottler competition producing higher rebates to retailers, we find it more likely that this substantial increase in promotional costs occurred because, without the Dr Pepper franchise, Big Red was being required to pay more for promotions.[331] Retailers expect better offers on ad features from bottlers whose products do not sell as much volume as those of other bottlers; as Mr. Kaiser of Kroger testified: "Generally Pepsi will offer more than Coke [on ad feature payments per case] because they don't sell as much product."[332] Thus, in addition to making it more difficult for Grant-Lydick to obtain ad features at all, the loss of the Dr Pepper franchise increased the cost to Grant-Lydick of competing against Coke and Pepsi in obtaining ad features -- the most significant means by which to obtain increased sales.[333]

c. The Likely Competitive Effects

The evidence demonstrates that CCSW's acquisition of the Dr Pepper franchise significantly impaired the ability of Big Red Bottling to compete with Coke and Pepsi for ad features, the form of competition that generates by far the largest volume of sales for branded CSD bottlers and retailers. This diminished ability to compete in such an important arena of branded CSD competition would

[328] CX 1697 G.

[329] Goode, Tr. 7424; RX 200; RX 201.

[330] RRCCPFF paragraph 2047 (citing RX 200); CX 4056.

[331] The evidence that shows increased promotional costs for branded CSD bottlers relates to the post-1986 time period, not to the 1983-86 time frame. *See, e.g.*, IDFF paragraph 172, 173, 309.

[332] Kaiser, Tr. 3210. *See also* CX 129, CX 3814 at 28-29 [Adams].

[333] *See* Section IV.C.3 *supra*.

likely reduce Big Red Bottling's incentives and ability to contest any anticompetitive branded CSD price increases. Therefore, we focus next on whether the other evidence similarly indicates a likelihood of anticompetitive effects, or whether it provides sufficient grounds for rebutting the presumption of anticompetitive effects that has been created by the degree of increased concentration in the relevant market.

3. The Increased Likelihood of Tacit Collusion in All Branded CSD Channels

As we have previously noted, "[t]he effective coordination of price and output strategies requires developing a consensus concerning price and output levels, and a means of enforcing its terms." *B.F. Goodrich*, 110 FTC at 294. However, collusion may occur without firms reaching complex terms concerning price and output levels.[334] "Instead, the terms of coordination may be imperfect and incomplete -- inasmuch as they omit some market participants, omit some dimensions of competition, omit some customers, yield elevated prices short of monopoly levels, or lapse into episodic price wars -- and still result in significant competitive harm." Merger Guidelines, Section 2.11.

Factors relevant to an evaluation of the likelihood of collusion include: the extent to which market information is available to market participants; whether there is a history of collusion in such markets; the number of market participants; the pricing and marketing practices used by market participants; the characteristics of sellers and buyers; and the heterogeneity (or lack thereof) of products and market participants.[335] We begin with an examination of the availability of market information to branded CSD bottlers.

a. Availability of Pricing Information

The evidence in this record indicates that branded CSD bottlers have access to key information about their competitors' prices and

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[334] Merger Guidelines, Section 2.11. For example, coordinating firms may "follow simple terms such as a common price, fixed price differentials, stable market shares, or customer or territorial restrictions." Merger Guidelines, Section 2.11.

[335] Merger Guidelines, Section 2.1.

promotions, and that retailers provide such information. The availability of this information could facilitate collusion.

For example, bottlers are aware of their competitors' wholesale prices because they can obtain pricing information "from a retailer or from some other source." Clarke, Tr. 4424. CCSW obtained a copy of Pepsi's 1987 Cooperative Marketing Program for Independent Grocery chains in the San Antonio area.[336] CCSW was shown a copy of Pepsi's proposed 1988 Ad Buy Program to J's Convenience Store chain by J's personnel.[337] CCSW obtained a copy of a Pepsi-Cola eight-week summer 1988 promotion with the Payless convenience store chain.[338] CCSW routinely collects and aggregates information regarding Pepsi's ad and instore retail prices.

One incident is particularly telling. In January, 1989, CCSW personnel obtained a copy of the carbonated soft drink promotional materials for National Convenience Stores, Inc. ("NCS"), which owns Stop-N-Go. CX 465; Hiller, Tr. 5367. Included in the materials was Pepsi's wholesale price to NCS in the San Antonio area. CX 465 B. When NCS confronted CCSW about the materials, James Doege of CCSW was quoted as stating that "all of my sales people bring [such] information in all of the time." CX 465 A.

Indeed, the day-to-day interactions with retailers that are necessitated by use of the DSD delivery system mean that branded CSD bottlers have the opportunity for almost immediate market information about their competitors, marketing, promotions, and pricing. The easy availability of such information suggests that any deviations from a collusive agreement could be quickly detected, thus enabling quick retaliatory action.

b. Branded CSD Pricing in San Antonio

Respondents contend that soft drink price competition in San Antonio has been fierce since the acquisition,[339] and that we should

[336] CX 87. CCSW admitted this, but denied any interference that it was obtained from Pepsi. RRCCPFF paragraph 1874.

[337] CX 2007D.

[338] CX 87. CCSW admitted this, but denied any inference that it was obtained from Pepsi. RRCCPFF paragraph 1872.

[339] ABR-A at 74. Respondent cites evidence that: after adjustment for inflation, soft drink prices in San Antonio have declined "significantly" since 1984 [IDFF paragraph 307]; that this real decline in soft drink prices has occurred while production and promotion costs were increasing [IDFF paragraph

take such evidence as confirming that collusion is unlikely.[340] We agree that the record does not contain any evidence of express collusion among branded CSD bottlers in the San Antonio market, and that the record shows a period of particularly deep discounting by both Pepsi and Coke in San Antonio in 1987.[341] However, this is not surprising, given the level of antitrust scrutiny that has been applied to the relevant market since the acquisition. In September, 1984, the Texas Attorney General's Office filed suit to challenge the transactions whereby CCSW acquired the Dr Pepper and Canada Dry franchises, alleging that the transactions violated Texas antitrust law.[342] On July 1, 1986, CCSW, DPUSA, and the Texas Attorney General entered into a settlement agreement applicable until July 1, 1993, which prohibited CCSW from certain activity -- such as seeking or accepting more than 65% of the shelf space "regularly allocated for the sale of soft drinks" in any store -- during that period of time.[343] In 1987, the Federal Trade Commission began its investigation of the acquisition, and its original complaint was filed on July 29, 1988.[344] In light of the intensive antitrust scrutiny at both the state and federal levels, it would be most surprising to find anything other than competitive conduct.

Moreover, although there is no evidence of express collusion, there is some evidence of the kind of price leadership that typifies an

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309]; that the Shircliff Report, plus other evidence (Campbell, Tr. 1950-51; Turner, Tr. 979; Trebilcock, Tr. 5874-75), establish that soft drink prices in Texas are among the lowest in the United States [IDFF paragraph 313-14]; and that fierce price competition in San Antonio drove CCSW into financial difficulty [IDFF paragraph 322].

[340] *See* ABR-A at 59.

[341] *See* Section IV.D.3 *supra.*

[342] CX 2 A-B; IDFF paragraph 67.

[343] CX 2 E. Among other things, the Settlement Agreement also prohibited CCSW from "seeking or consenting to participate in, on the average, more than 65% of" promotional ads during any calendar year, or seeking or accepting "exclusive end-of-aisle display space" for "more than 65% of the weeks in any given calendar year." IDFF paragraph 68.

The ALJ found that the provisions of this Settlement Agreement imposed constraints on CCSW's use of marketing programs and practices in the San Antonio area, and that the Texas Attorney General's office had the authority and incentive "to deter any collusive price increase by CCSW." IDFF paragraph 462. In light of this, as well as his assessment of other evidence, the ALJ found that collusion seemed unlikely. ID 77.

We do not rely on the Settlement Agreement to constrain CCSW's market conduct, because it expired on July 1, 1993; although the Texas Attorney General is entitled to seek an extension of the order for a period of up to three years, CX 2-H, VIII, there is no record evidence to indicate that the Attorney General has sought and obtained such an extension.

[344] IDFF paragraph 43.

oligopolistic market susceptible to tacit collusion.[345] That is, as we discuss in detail below, it appears that each branded CSD bottler in San Antonio, acting individually, has copied the price of the price leader in the market at certain times. As then-Judge (now Justice) Stephen Breyer has explained:

> Courts have noted that the Sherman Act prohibits agreements, and they have almost uniformly held, at least in the pricing area, that such individual pricing decisions (even when each firm rests its own decision on its belief that competitors will do the same) do not constitute an unlawful agreement under Section 1 of the Sherman Act. . . . That is not because such pricing is desirable (it is not), but because it is close to impossible to devise a judicially enforceable remedy for 'interdependent' pricing. How does one order a firm to set its prices without regard to the likely reactions of its competitors?[346]

Based on the record before us, we have no reason to believe that the price leadership that we observe in the San Antonio branded CSD market -- as described below -- is anything other than legal. But we do not view such pricing as desirable, and an acquisition that may substantially increase the likelihood of interdependent pricing in a market that already appears susceptible to such pricing may have anticompetitive consequences.[347]

As CCSW itself recognizes, "Coke is typically the price leader in the San Antonio market." CX 3806 G.[348] David Davis of Pepsi agrees: "Coke is usually the leader in the market. They go up, and then we usually follow, depending on our pricing structure." Davis,

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[345] *See, e.g., Clamp-All Corp. v. Cast Iron Soil Pipe Institute*, 851 F.2d 478 (lst Cir. 1988) (Breyer, J.), *cert. denied*, 488 U.S. 1007 (1989) (oligopolistic pricing, including price leadership, is not competitively desirable) ("Clamp-All"). One of the purposes of the Clayton Act Section 7 is to prevent markets from becoming oligopolistic and thus susceptible to coordinated interaction, which "includes tacit or express collusion, and may or may not be lawful in and of itself." Merger Guidelines, § 2.1.

[346] Clamp-All, 851 F.2d at 484 (emphasis in original) [citations omitted].

[347] The Merger Guidelines explain that a merger may diminish competition by enabling firms more likely, more successfully, or more completely to engage in coordinated interaction that harms consumers." Section 2.1. The Merger Guidelines define coordinated interaction as "actions by a group of firms that are profitable for each of them only as a result of the accommodating reactions of the others." *Id.* "This behavior includes tacit or express collusion, and may or may not be lawful in and of itself." *Id.* (emphasis added). Thus, the Merger Guidelines make clear that a merger may violate the FTC and the Clayton Acts because, among other things, it substantially increases the likelihood of tacit collusion that may be legal in and of itself.

[348] This statement appears in a Texas Bottling Group ("TBG") presentation to its Credit Committee. CX 3806. While noting that "TBG encounters aggressive competition from Pepsi," the document notes Coke's price leadership as a "mitigator." CX 3806 G. The reference to price leadership is particularly telling, given the ALJ's observation that statements in this document were likely influenced by litigation considerations. ID 67.

Tr. 4532. Emery Bodnar of Grant-Lydick reports the same: "I would say from where I sat, my price increase was pretty much dictated on when Coke increased, I followed as quickly as possible." Bodnar, Tr. 1356.

The record contains examples of such price leadership. For example, in February 1989, CCSW initiated a 6% wholesale price increase.[349] Big Red Bottling matched immediately in mid-February, followed by Pepsi on March 1.[350] Texas Bottling Group, CCSW's owner, projected that CCSW's 1989 price increase would bring increased sales: "A 6.0% increase in net price per case coupled with a shift in production mix will yield a 10.8% increase in sales in 1989." CX 3806 Z-6.[351]

It appears that such price leadership may have taken place even before this acquisition. Mr. Bodnar's testimony indicates that DPSA also followed Coke's lead on price increases.[352] After the acquisition, there was a substantially increased probability that Big Red Bottling Company would play the "follower" role, since it had lost the Dr Pepper franchise (and thus Dr Pepper sales volume) to CCSW.[353] Indeed, the market might have become more competitive if the Dr Pepper franchise had remained combined with the RC franchise, the

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[349] CX 3806 Z-56.

[350] CX 3806 Z-56.

[351] The ALJ stated that CCSW tried to raise list prices in 1989, but was forced to discount prices back to former levels due to lost sales. ID 69. We have not found any record evidence to show that CCSW rolled back its 1989 price increase. The ALJ also stated that the Pepsi COBO "unsuccessfully" tried to raise its prices in 1989, allegedly losing 19% of its Nielsen share during the first seven months of 1989. ID 69; IDFF paragraph 410. Again, we can find no record evidence that Pepsi ever rolled back its 1989 price increase. Thus, we have no basis on which to regard the price increase as "unsuccessful;" indeed, we presume that, if the Pepsi COBO stayed with the price increase for an extended period of time, it did so because it was profitable, despite any volume loss that might have been associated with it.

Finally, the ALJ looked to the profitability of CCSW's 1989 price increase as evidence indicating that the current market is competitive. The ALJ stated that, in 1989, CCSW raised its list price by $.69 per case, but over the year had a net profit increase of only $.01 per case, ID 69; IDFF paragraph 409, and that CCSW was unable to raise its prices as much as would have been necessary to account for cost increases. IDFF paragraph 409. But the issue is not whether the current market is competitive. Given the intense and ongoing antitrust scrutiny of this market, we would be surprised if it were not competitive. The issue here is whether this acquisition has taken place in a market susceptible to collusion. The price leadership shown in the 1989 price increase is one piece of evidence indicating that the market is susceptible to collusion.

[352] Bodnar, Tr. 1356.

[353] *See* Section VI.C.2 *supra*.

combination that Mr. Bodnar described as giving DPSA critical mass.[354]

In sum, we find that the price leadership by CCSW evident in the relevant market supports an inference that the market is susceptible to interdependent pricing -- that is, tacit collusion -- and that the evidence concerning Big Red Bottling's diminished ability to compete with respect to ad features demonstrates that CCSW's acquisition of the Dr Pepper franchise substantially increased the likelihood that Big Red Bottling would continue to follow CCSW's price leadership.

c. Collusion by Branded CSD Bottlers

There have been over 40 price-fixing cases involving branded CSD bottlers in a number of local geographic markets.[355] Complaint counsel offered evidence relating to these collusion cases, but the ALJ rejected it as irrelevant.[356] We find the evidence to be relevant to the likelihood of collusion by branded CSD bottlers in the San Antonio market, because such cases suggest that there are local or regional branded CSD bottling markets that are conducive to collusion.[357] The cases suggest that, in markets structured similarly

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[354] *See* Section VI.C.2.a *supra.*

[355] *See, e.g.*, Convictions: *United States v. Mid Atlantic Coca-Cola Bottling Co.*, 6 Trade Reg Rep. (CCH) paragraph 45,090 (E.D. Va. 1990); *United States v. Allegheny Bottling Co.*, 695 F. Supp. 856 (E.D. Va. 1988), *aff'd*, 870 F.2d 656 (4th Cir. 1989); *United States v. Hartford*, [1988-21 Trade Cas. (CCH) paragraph 68,386 (4th Cir. 1989); *United States v. Gravely*, 840 F.2d 1156 (4th Cir. 1988). Guilty pleas: *United States v. Pepsi-Cola Bottling Co. of Walla Walla*, No. CR-89-394-01 (E.D. Wash., Jan. 16, 1990); *United States v. Coca-Cola Bottlina Co., Yakima and Tri Cities*, No. CR 89-372-01 (E.D. Wash. Jan. 16, 1990); *United States v. Blue Mountain Bottling Co. of Walla Walla*, No. CR 89-392-01 (E.D. Wash. Jan. 16, 1990), aff'd, 929 F.2d 526 (9th Cir. 1991); *United States v. Rice Bottling Enterprises, Inc.*, No. 3-89-72 (E.D. Tenn., Oct. 16, 1989); *United States v. Pelpsi-Cola Bottling of Petersburg, Inc.*, No. 89-00062 (E.D. Va., Oct. 11, 1989); *United States v. Atlantic Soft Drink Co.*, No. 3-88-77 (E.D. Tenn., Dec. 23, 1988); *United States v. Beverage South, Inc.*, No. 88-451 (D.S.C., Dec. 2, 1988); *United States v. All-American Bottling Corp.*, No. 88-00038 (W.D. Va., Apr. 12, 1988); *United States v. Coca-Cola Bottling Co. of Roanoke, Va.*, No. 88-00012 (W.D. Va., Apr. 15, 1988); *United States v. Akron Coca-Cola Bottling Co.*, No. CR 88-044 (N.D. Ohio, March 15, 1988); *United States v. Seven-Up/Dr Pepper Bottling Co.*, Beckley, W. Va., No. 88-00012 (W.D. Va., Feb. 1, 1988); *United States v. NEG Holding Co.*, No. CR 87-16-01 (N.D. Ga., Nov. 24, 1987); *United States v. Mid Atlantic Coca-Cola Bottling Co.*, No. 87-0420 (D.D.C., Oct. 14, 1987); *United States v. General Cinema Beverages of Washington, D.C.*, No. CR 86-0352 (D.D.C., Oct. 15, 1986).

[356] RCX 3323-52; 3354; 3356-57; 3359-65; 3367-68; 3788; 3950; Tr. 114-17, 470-72, 4101-05, 4141, 6089-97, 6176, 6341-45, 6937-40, 8417-22.

[357] *See* Coca-Cola, slip op. at 48. In that case, we found evidence of branded CSD bottler collusion relevant to an assessment of the likelihood of collusion by a cartel of branded CSD concentrate companies, because it suggested that, if such a cartel raised concentrate prices nationally, bottlers could successfully pass on the price increase. *Id.*

to the San Antonio market,[358] branded CSD bottlers have perceived that "the number of competitive dimensions involved posed no insuperable obstacle to collusion." Coca-Cola Co., slip op. at 48.[359] The bottler price-fixing cases also are relevant to and reinforce our conclusion that the relevant market in this case is branded CSDs in the San Antonio market.[360]

The branded CSD bottler collusion cases provide evidence of actual collusive conduct that negates the hypothetical difficulties in colluding that respondent raises. Respondent argues that "the variety of brands, packages, flavors, sweeteners, and advertising support" for soft drinks complicates the market sufficiently to deter collusion.[361] However, the same type of variety exists in the markets in which branded CSD bottler collusion took place and apparently did not deter that collusion.[362] Indeed, the bottler collusion cases and the bottler documents in the record here suggest that factors such as

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358 As we found in Coca-Cola Co., "[m]ost local markets for carbonated soft drinks have a Coca-Cola bottler, a Pepsi-Cola bottler, and a so-called 'third bottler,' which carries various brands of soft drinks other than Coca-Cola or Pepsi-Cola brands." Slip op. at 57. The record here similarly supports this finding. *See also* Lydick, Tr. 2937, 2943. "[A] record of price fixing or other antitrust violations is some evidence that the structure of the market is favorable to collusion." R. Posner, Antitrust Law: An Economic Perspective 55-61 (1976).

359 Under the Merger Guidelines, "[p]revious express collusion in another geographic market will have the same weight [as express collusion in the same geographic market] when the salient characteristics of that other market at the time of the collusion are comparable to those in the relevant market." Section 2.1. Here, the bottler collusion cases arose from a variety of areas in the United States, suggesting that the salient characteristics that facilitate collusion among branded CSD bottlers are not unique, but instead are present in typical local branded CSD bottling markets. This is not surprising, since the basic structure of local branded CSD bottling markets in the United States tends to be only three branded CSD bottlers using DSD delivery. Lydick, Tr. 2937, 2943. This trend follows a significant period of bottler consolidation. In 1960 there were 4,519 soft drink bottling operations in the United States, in 1970 there were 3,054, and in 1980 there were only 1,960 (CX 996 A), and in 1983 there were only 1,500. CX 3218 M.

Moreover, the branded CSD bottler price-fixing cases are far more relevant to this case than the discussion of the OPEC cartel permitted by the ALJ. *See* Strickland, Tr. 8283-85. Given the direct relevance of the bottler collusion cases to this market, we find that the ALJ erred in refusing to admit this evidence.

360 The colluders in these cases were bottlers of branded CSDS, and the actual price increases typically were maintained for over one year. *See* cases in note 355 *supra; e.g., Allegheny Bottling Co.*, 695 F. Supp. at 858. The cases usually identified discrete, local geographic markets of no more than twelve counties and as few as one, far less than the 107 counties proposed by respondent as the relevant geographic market in this matter. CX 4131; *see* IDFF paragraph 246.

361 ABR-A at 63

362 *See generally* Section IV.D.3.c *supra* (documents and testimony from national concentrate companies indicate same general competitive conditions in terms of brands, packages, flavors, sweeteners, and advertising support for all of their bottlers). *See also* Lydick, Tr. 2937, 2943.

standard packaging ease price comparisons, which can facilitate collusion.[363]

Respondent also argues that "[t]he putative colluders, in addition to devising a complicated set of list prices, net prices, and net, net prices, would also have to control promotional programs so that volume changes would not disrupt each colluder's expectation of bottom-line profit." ABR-A at 64. But participants to some of the collusive schemes have fixed prices successfully simply by agreeing not to offer discounts on various products.[364]

In sum, the branded CSD bottler price-fixing cases reinforce our previous conclusions that collusion need not be perfect to be successful and that the relevant market in this case is susceptible to collusion.

4. Respondent's Arguments Against the Likelihood of Collusion

Respondent presents a variety of additional arguments that supposedly negate any inference of an increased likelihood of collusion, tacit or express, following CCSW's acquisition of the Dr Pepper franchise. As we discuss below, we find these arguments unconvincing.

a. Differing Profit Incentives Among Bottlers

Respondent argues that CCSW, the Pepsi COBO, and Grant-Lydick all have differing profit incentives, and that such differing incentives could hamper collusion. ABR-A 61. Respondent points out that the Pepsi COBO is owned by Pepsi USA, and that Pepsi USA makes a 96% gross profit on concentrate sales.[365] By contrast, respondent states that CCSW makes no profit on CCUSA's concen-

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[363] For example, RX 582, entitled "1987 Pricing Summary," shows that price comparisons are relatively easy, given standardized packaging.

> For the periods of November and December, we are at parity on in-store pricing and at parity on ad feature pricing for the 2 liter and 3 liter non-holiday and one price unit disadvantaged versus Pepsi on cans non-holiday. For the holidays of November and December, we were at parity on 2 liter. We are one price unit disadvantaged on cans.

This document reflects quite simple comparisons, not complexity.

[364] *Hartford*, 1988-2 Trade Cas. (CCH) paragraph 68,386 at 60,131; *Allegheny Bottling Co.*, 695 F. Supp. at 857.

[365] CX 3913.

trate sales.[366] Even CCSW and Grant-Lydick are dissimilar, in that Grant-Lydick purchases its cans from an independent packer,[367] whereas CCSW provides its own cans.[368]

Respondent is correct that such differing profit incentives may operate to make collusion more difficult. However, we must evaluate the evidence as a whole, and we are not convinced that such differing profit incentives, even in combination with other factors present here, would be sufficient to deter collusion in this market. For example, Mr. Davis of Pepsi has acknowledged that Pepsi's strategy in San Antonio is now focused on profitability rather than on increasing market share, as was the case during the deep discounting period of 1987-88.[369] An emphasis on profitability rather than market share may increase the likelihood of collusion.[370]

As to Grant-Lydick, the fact that Grant-Lydick's higher can costs provide it with a greater incentive than CCSW has to keep can prices high only suggests that it would favor a collusive agreement on can prices rather than another type of agreement. This argument alone does not demonstrate that collusion is unlikely in the relevant market; in fact, it might make collusion more likely.

b. Differing Size Firms

Respondent also asserts that the range of firm size in this case -- which may produce different cost structures for each firm -- renders collusion "highly improbable."[371] We agree that, in theory, differing cost functions among firms may make it more difficult for firms to agree on a consensus collusive price.[372] However, it would be a leap

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[366] Respondent cites R. Hoffman at Tr. 5577-78, but the citation does not support respondent's claim.

[367] Turner, Tr. 1117; Bodnar, Tr. 1526-27.

[368] Summers, Tr. 6403-04.

[369] Davis, Tr. 4527-28.

[370] Respondent notes that none of the bottler collusion cases tendered by complaint counsel involved a Pepsi COBO. ABR-A at 62 n.53. We do not find that this absence renders those cases irrelevant, however. We note that San Antonio is one of Pepsi's worst markets -- a market in which Pepsi's share increased only from 15% to 19% after a year and one-half of losing millions of dollars from offering extraordinarily low prices. Davis, Tr. 4548-4565. After such an experience, the Pepsi COBO could well become more interested in collusive -- and profitable -- price increases than in continuing vigorous price competition.

[371] ABR-A 60-61.

[372] *See B.F. Goodrich*, 110 FTC 207, 321 (1988).

of faith, given a lack of supporting analysis in the record, to decide that the different cost structures present here constitute a significant obstacle to collusion in this highly concentrated market. In addition, CCSW's apparent role as price leader and the possible benefits to reaching and maintaining a collusive agreement suggest that this dominance may be an offsetting force acting for rather than against collusion.

D. Unilateral Anticompetitive Conduct

An acquisition may diminish competition by making it profitable for a firm to alter its behavior unilaterally by elevating price and/or suppressing output.[373] This phenomenon may occur in markets where products are differentiated by flavor, among other things.[374] Thus, an acquisition may enable the acquiring firm to raise the price of either its original product, or the acquired product, or both above the premerger level. As explained in the Merger Guidelines, "[s]ome of the sales loss due to the price rise merely will merger partner and, depending sales loss through merger may even though it would not have success of this strategy will significant share of sales in be diverted to the product of the on relative margins, capturing such make the price increase profitable been premerger." Section 2.21. The success of this strategy will require that "there be a significant share of sales in the market accounted for by consumers who regard the products of the merging firms as their first and second choices, and that repositioning of the nonparties' product lines to replace the localized competition lost through the merger be unlikely." Merger Guidelines, Section 2.21.

In this case, CCSW may have been constrained from taking some anticompetitive actions due to concern about ongoing antitrust litigation and certain restrictions imposed as part of CCSW's settlement with the Texas Attorney General.[375] Nonetheless, there is some evidence of unilateral effects that have occurred since the acquisition of the Dr Pepper franchise. We begin by examining this evidence --

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[373] Merger Guidelines, Section 2.2.

[374] Merger Guidelines, Section 2.21.

[375] For example, among other things, the Settlement Agreement prohibited CCSW from "seeking or consenting to participate in, on the average, more than 65% of" promotional ads during any calendar year. CX 2 E; IDFF paragraph 68. *See also* n. 343 *supra*.

which involves the elimination of take-home sales of Mr. PiBB and a lessening of competition in the vending channel -- and then briefly discuss the potential for further effects with respect to ad features based on CCSW's increased market power.

1. The Elimination of Competition Between Mr. PiBB and Dr Pepper

CCUSA and Dr Pepper Company are the only firms in the soft drink industry that have a viable "pepper" category soft drink.[376] The Dr Pepper Company sells Dr Pepper concentrate; CCUSA sells concentrate for Mr. PiBB.[377]

Mr. PiBB was introduced by CCUSA in 1973. RX 888 D. As CCSW has admitted,[378] CCUSA defined the consumer role of Mr. PiBB as the "Alternative to Dr Pepper."[379] In 1984, CCUSA defined the business role of Mr. PiBB as "Competitor to Dr Pepper," CX 1895B, designed to "combat" the brand:

> Mr. PiBB represents the only viable alternative to Dr Pepper in its flavor category. The brand is necessary, especially in cold drink, to enable bottlers to combat Pepper where it is strong.

CX 791 C. CCUSA targeted Dr Pepper consumers with its Mr. PiBB brand.[380]

Prior to CCSW's acquisition of the Dr Pepper franchise, Mr. PiBB was sold in San Antonio, as was Dr Pepper.[381] CCSW'S business records reveal that CCSW viewed Mr. PiBB as the closest substitute to and a direct competitor of Dr Pepper,[382] and considered Mr. PiBB to be one of its major sugar brands.[383] San Antonio was a

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[376] CX 791C; CX 790.

[377] CX 790 B; CX 791 B, S; RX 888 C-D.

[378] RRCCPFF paragraph 2098.

[379] CX 1895 A; CX 790; CX 791. Mr. PiBB is perceived in the marketplace as a "me-too" brand. CX 791 E.

[380] CX 1885; CX 1898 B; CX 1896; CX 1894; RX 888 D; Turner, Tr. 954; Clarke, Tr. 4278, 4400-01; CX 1893.

[381] Turner, Tr. 996; Bodnar, Tr. 1361; Schwerdtfeger, Tr. 2327, 2344; Anderson, Tr. 3850.

[382] CX 596.

[383] CX 510 R; CX 3480 E; CX 3481 E.

priority market for Mr. PiBB.[384] CCSW's sales of Mr. PiBB were above the national average,[385] and San Antonio accounted for 3% of all Mr. PiBB volume in the United States.[386]

In 1983, Mr. PiBB's market share was 2.1%, and Dr Pepper's share was 8.4%.[387] After the acquisition, CCSW no longer sold Mr. PiBB in bottles and cans in the territory in which Dr Pepper was sold.[388] Mr. Hoffman testified that the elimination of Mr. PiBB occurred because it was a competing flavor with Dr Pepper, and flavor restrictions from the Dr Pepper Company prohibited CCSW from selling a competitive flavor.[389]

Although there was testimony that CCUSA would consider licensing another distributor to distribute Mr. PiBB in San Antonio, this has not happened.[390] After CCSW stopped distributing Mr. PiBB in the take home market in San Antonio, Dr Pepper's market share began increasing; but only in 1987 did Dr Pepper's market share come close to the combined 1983 share of Dr Pepper and Mr. PiBB.[391]

Most significantly, after the acquisition, CCSW raised the wholesale price of Dr Pepper to parity with CCSW's other products.[392] Other data show that retail prices of Dr Pepper in San Antonio, which prior to the acquisition had been below the national average of Dr Pepper prices, after the acquisition rose to above the national average

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384 CX 792 G.

385 CX 3837 B, G.

386 CX 792 L; CX 1897 E. San Antonio also accounted for 9.5% of the CCUSA PiBB brand funding in 1983 and 7.6% of funding in 1982. CX 792 L. In fact, Mr. PiBB's BDI (Brand Development Index [CX 591 Cl) in San Antonio was the highest in the nation. CX 792 0.

387 CX 1681 C. These market shares are based solely on sales of bottles and cans, since that is the channel of sales that was eliminated. *See* Hilke, Tr. 6030, 6033. (CX 1681 uses Nielsen data for soft drink sales in food stores in Bexar County, which includes San Antonio).

388 Anderson, Tr. 3879, 3859; CX 596 A-I; CX 2192; Atchison, Tr. 5252; CX 3221 A. CCSW has continued to sell Mr. PiBB postmix syrup. CCSW also sells Mr. PiBB outside of its Dr Pepper franchise area.

389 E. Hoffman, Tr. 324, 421; CX 122.

390 *See* Atchison, Tr. 5252-54.

391 Data show the 1983 combined share of Dr Pepper (8.4%) and Mr. PiBB (2.1%) for bottle and can sales in San Antonio as about 10.5%. CX 1681 C. Dr Pepper's share for bottle and can sales reached 9.1% in San Antonio in 1987. CX 1681 C.

392 CX 563 E.

for Dr Pepper retail prices.[393] In 1989, in a telling memorandum from Mr. Summers to Messrs. E. and R. Hoffman, Mr. Summers stated: "We are pricing Dr Pepper one increment above other brands on in-stores, since it has no competition in its flavor segment." CX 2261; Summers, Tr. 686870.

Dr Pepper had no competition in its flavor channel -- and therefore was priced higher in 1989 than it otherwise would have been -- because Mr. PiBB had been eliminated as a competitive option for consumers in San Antonio, as a result of the acquisition at issue in this case. Consumers in the San Antonio area who preferred Mr. PiBB to other bottler or canned soft drinks were placed in the position of having to switch to less-desirable alternatives and, as a result, were made less well-off.

2. CCSW's Increased Market Power Over Vending Machine Sales

The record demonstrates that, post-acquisition, the choices available to consumers from vending machines were reduced, and the prices charged to third-party vendors increased. There was testimony that, prior to the acquisition, third-party vendors had been able to resist any attempt by a branded CSD bottler to force a vendor to take unwanted allied brands along with the desired brands.[394] About three or four years after the acquisition, however, CCSW imposed a requirement that a third-party vendor cannot qualify for the best available discount unless 20% of its purchases are allied brands such as Sprite, Sunkist, and Hires.[395] Ladd Little of LV Vending attributes CCSW's ability to impose the requirement to its acquisition of the Dr Pepper franchise.[396] Because of this requirement, he purchases Sprite, Sunkist, and some other flavors from CCSW, while he would prefer to purchase 7-Up and Crush from Grant-Lydick and Slice from Pepsi.[397] In addition, Mr. Little testified that, post-acquisition, Dr

[393] CX 1685 A, E-H; Hilke, Tr. 6252-53, 6288-89.

[394] Prior to the acquisition, CCSW did not require third-party vendors to accept allied brands in order to get the desired brands; Pepsi had attempted to impose such a requirement without success. Little, Tr. 667-68, 705.

[395] Little, Tr. 665-66.

[396] Little, Tr. 665, 705.

[397] Little, Tr. 668-69, 704.

Pepper case prices increased to the level of the Coke case prices.[398] The unilateral effect in this instance appears to be CCSW's ability to increase price either directly (by raising case prices of Dr Pepper) or indirectly (by tying purchases of other, less attractive products to discounts on attractive products).

3. CCSW's Increased Market Power Over Ad Features

As noted above, the acquisition of the Dr Pepper franchise increased CCSW's ability to obtain ad features and thus increased CCSW's market power.[399] The evidence suggests that CCSW obtained more feature ads after its acquisition of the Dr Pepper franchise than it had previously.[400] The increased "pull" of all of CCSW's brands gives CCSW the potential power to extract more favorable deals from retailers and to disadvantage both the Pepsi COBO and Big Red Bottling in their attempts to obtain ad features.[401] In addition, CCSW's increased market power may have contributed to its ability to raise Dr Pepper's price. *See* also Section VI.C.2 *supra.*

E. Power Buyers

Respondent argues that there are power buyers who could constrain any collusive or unilateral attempt by branded CSD bottlers to raise price. The ALJ agreed, stating that, in the face of a price rise among national CSD brands, retailers such as H.E.B., Kroger, and others who stock their own private label brands "could easily promote those brands in place of national brands." ID 76.[402]

398 Little, Tr. 669-70.

399 Market power includes the ability to "lessen competition on dimensions other than price, such as product quality, service, or innovation." Merger Guidelines, Section 0.1 & n

400 *See* CX 2954 H (in 1984, some of Dr Pepper's feature ads took place before the acquisition whereas all of Dr Pepper's feature ads are attributable to CCSW). DPUSA recognized the advantages of being advertised with Coke and advised that Dr Pepper should be advertised with Coke to build sales, RX 2825 C.

401 The record shows that Pepsi already generally has to offer more ad feature payments to a retailer than Coke because Pepsi doesn't sell as much product. Kaiser, Tr. 3210; *see also* CX 129; CX 3814 at 28-29 [Adams].

402 The ALJ also found that concentrate companies such as CCUSA, Pepsi USA, and DPUSA had "the power and the incentive to deter collusion at the bottler level." ID 76-77. We find that the numerous bottler collusion cases listed earlier, *see* note 355 *supra*, provide sufficient evidence to undermine any hope we might have that concentrate companies could prevent collusion in this market; the concentrate companies did not prevent collusion by the bottlers in those cases.

In analyzing the competitive effects of a merger, both the Commission and the federal courts have considered the possible power of buyers in deterring anticompetitive effects.[403] The relevant market here does contain large buyers who are large food retailers. H.E.B., the largest buyer, accounts for approximately 25% of CCSW's take-home sales and approximately 20-25% of Pepsi's take-home sales.[404] Kroger is the second largest customer of CCSW, purchasing from 9-12% of CCSW's total unit sales.[405] Sam's Wholesale Clubs purchase 7-8% of CCSW's total unit sales.[406] In addition to the leverage that may be provided by such sales volumes,[407] retailers have some leverage over branded CSD bottlers because the retailers can control the availability of their own ad features and in-store displays, which can be important to the marketing of the branded CSDs of the bottlers.[408]

Just to note these facts does not demonstrate that retailers in this market could constrain any anticompetitive price increases, however. Rather, we must analyze the extent to which retailers facing an anticompetitive price increase could avail themselves of options other than paying the price increase and thereby force the branded CSD bottlers to return to a competitive price:

> Consideration of large and sophisticated buyers generally focuses on the buyers' ability to exert countervailing power, even against a seller's oligopoly, by (1) shifting a large proportion of business to any firms that are willing to deviate from the coordinated behavior; (2) inducing new entry into the oligopolized market; or (3) through vertical integration.

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403 *See, e.g.*, Adventist Health System/West, Dkt. No. 9234 (Apr. 1, 1994), Concurring Opinion of Commissioner Owen and Commissioner Yao, slip op. at 16-19; Owens-Illinois, Inc., Dkt. No. 9212, 5 Trade Reg. Rep. Rep. (CCH) paragraph 23,162 (FTC 1992); Olin Corp., Dkt. No. 9196, 5 Trade Reg. Rep. (CCH) paragraph 22,857 (FTC 1990); *United States v. Baker Hughes, Inc.*, 908 F.2d 981 (D.C. Cir. 1990); *United States v. Syufy Enterprises*, 903 F.2d 659 (9th Cir. 1990); *United States v. Archer-Daniels-Midland Co.*, 1991-2 Trade Cas. (CCH) 1 69,647 (S.D. Iowa 1991); *United States v. Country Lake Foods, Inc.*, 754 F. Supp. 669 (D. Minn. 1990).

404 CX 3806 Z37; Summers, Tr. 6589; Davis, Tr. 4525; IDFF paragraph 432.

405 Summers, Tr. 6589; IDFF paragraph 433.

406 Summers, Tr. 6638; IDFF paragraph 435.

407 We note, however, that the size of these alleged "power buyers" falls far short of that in Country Lake Foods, where the three largest distributors accounted for more than 90% of sales. 754 F. Supp. at 674.

408 Coyne, Tr. 3449-52, 3487; Turner, Tr. 1130-31; IDFF paragraph 171, 445. As we discussed earlier, ad features and in-store displays are extremely important to increasing sales of branded CSDs. *See* Sections IV.C.3, VI.C.2 *supra*.

Adventist Health System/West, Dkt. No. 9234 (Apr. 1, 1994), slip op. at 16 (Concurring Opinion of Commissioner Owen and Commissioner Yao).[409]

As discussed below, we have considered these possibilities and have concluded that none appear to be realistic options for the retailers in this market. Moreover, we find that the instances of supposed buyer power cited by respondent and the ALJ do not suggest that the buyers in this market could successfully counter a collusive or unilateral price increase by branded CSD bottlers to retailers.

1. Shifting Purchases to Others

The ALJ found that H.E.B. and other retailers who sell their own private label soft drinks could switch to promoting those soft drinks instead of branded CSDs if confronted by a collusive price increase.[410] Our finding that private label soft drinks are not in the relevant market militates against this conclusion. As we have explained, the evidence shows that retailers depend on branded CSDs as a promotional item to draw in customers[411] and would not switch to purchasing nonbranded CSDs in the face of an anticompetitive price increase.[412]

The question then becomes whether H.E.B. and other retailers would switch to any firms within the market that would be willing to deviate from cartel conduct or undermine unilateral anticompetitive conduct. In this market, there are only three main bottlers making sales of branded CSDs to retailers: CCSW, Pepsi COBO, and Grant-Lydick (Big Red Bottling). The branded CSD products of these firms are differentiated, however, and are not exact substitutes for each other. Thus, we would expect that switching among branded CSDs would not always be costless for a retailer, and that under certain circumstances retailers might be reluctant to try to substitute exclusive ad features on Pepsi or Big Red for all ad features on Coke, for example.

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409 *See also Baker Hughes, Inc.*, 908 F.2d at 986-87; *Country Lake Foods, Inc.*, 754 F. Supp. at 679; *Olin Corp.*, 5 Trade Reg. Rep. (CCH) paragraph 22,857, at 22,553.

410 ID 76.

411 *E.g.*, CX 3806 Z37, ZSO; *see* Sections IV.C.3, VI.C.2 *supra*.

412 *See* Section IV *supra*.

In fact, the evidence indicates that, particularly with respect to Coke, retailers do not always regard branded CSDs as perfect substitutes. The assessment of TBG, owner of CCSW, was that although CCSW was dependent on the retail chains for increased volume of sales, "the chains are dependent on soft drinks as a promotional item to draw customers into their stores." CX 3806 Z37. And not just any "soft drink" would do. TBG noted that, although "H.E.B. has significant negotiating power," a "mitigating" factor is that "H.E.B. must buy Coke products from TBG in its franchise territories." CX 3806 G. According to TBG's own assessment, "[w]hile TBG may lose an occasional major ad to Pepsi, they believe that it is not in H.E.B.'s best interest, long term, to promote Pepsi products due to Pepsi's relatively weak market share (20% vs. 60% for TBG)." CX 3806 ZS 5.[413] Other evidence is consistent with TBG's analysis.[414]

This market share dominance of Coke over Pepsi also applies to Big Red, whose market share in food stores in 1984 was roughly

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[413] Similarly, in a 1987 antitrust suit against CCSW's parent, TBG, by Oneta Company, an independent Pepsi bottler in Corpus Christi, Texas, Toby Summers testified that CCSW made basically "take it or leave it" offers to accounts such as Albertson's:

Q. But I can't tell what the terms of a counter offer or negotiated ultimate agreement was from the terms of your proposal.

A. Well, whatever the ultimate agreement was would have been within the parameters of the proposal. These were not subject to negotiation. They were subject to,'this is the offer.' And then it became incumbent on the account to --

Q. They either took it, or they didn't.

A. -- avail themselves of the offer, or not to avail themselves of the offer. It was not a matter of negotiation.

CX 4021 at 678 [Summers]. *See Oneta Company v. Texas Bottling Group, Inc.*, No. C-87-97 (S.D. Texas - Corpus Christi Div.).

[414] James Nicholson of RC believes that the Coca-Cola brand is so important to retailers such as H.E.B. and Kroger that the retailers are reluctant to take actions that concern Coca-Cola bottlers. Nicholson, Tr. 3813-15.

The ALJ pointed to evidence that, in 1988, rather than risk retribution from H.E.B., CCSW had complied with H.E.B.'s notice that it would not accept price increases for four months. Summers, Tr. 6769; IDFF paragraph 449. But this notice from H.E.B. went to vendors for all products (not just soft drinks) and was applicable for only a short time, Summers, Tr. 6769, so we do not find that it constitutes convincing evidence of H.E.B.'s ability to disrupt a branded CSD bottler cartel. Perhaps more telling is the history of CCSW's negotiations with Stop-N-Go, a leading convenience store chain in the San Antonio area, regarding promotional programs. In 1986, Stop-N-Go refused to feature Coca-Cola products in South Texas for six to nine months, because CCSW would not agree to Stop-N-Go's terms for promotional programs. Howell, Tr. 4061-63; IDFF paragraph 450. The terms that CCSW wanted were exclusive promotions for Coke products. Bodnar, Tr. 1381. In 1987, Coke received exclusivity in exchange for adhering to Stop-N-Go's promotional terms. Moreover, in 1988, Coke persuaded Stop-N-Go to drop its promotional terms while maintaining the Coke ad features schedule for 1988. Bodnar, Tr. 1381. This history indicates that Stop-N-Go gave in to CCSW's demands, not the reverse, and may reflect the leverage that Coke's market dominance in the San Antonio market gives to CCSW.

comparable to but smaller than Pepsi's,[415] and even more compellingly to the other branded CSD products sold by Grant-Lydick and the Espinoza companies, none of whose shares reach even the 20% mark.[416] In the face of such market share dominance by Coke, we are skeptical that H.E.B. (or any other retailer) would switch all purchases to another branded CSD, since such a switch might well have a large impact on the retailer's overall sales of branded CSDs.[417]

Nor does it appear that H.E.B. (or any other retailer) has sufficient leverage over either Pepsi COBO or Grant-Lydick to force them to deviate from a possible collusive agreement. Mr. Davis of Pepsi COBO testified that H.E.B. does not have the clout to demand that Pepsi bottlers uniformly price their branded CSDs throughout H.E.B.'s sales territory, and that Albertson's had been unsuccessful in its attempts to convince Pepsi bottlers to price their branded CSDs uniformly throughout Albertson's sales territory.[418] Emery Bodnar testified that Grant-Lydick has never rolled back a wholesale price increase at the request of H.E.B., and that H.E.B. does not have the clout to force Grant-Lydick to rollback wholesale prices.[419]

In addition, this market does not feature the types of sporadic, large, and not immediately observable orders that encourage cheating on a cartel.[420] Although some retailers negotiate a promotion schedule of advertisements for an entire year, other large retailers -- such as H.E.B. -- decide on promotions in much smaller time periods.[421] Thus, the offers that branded CSD bottlers would make would involve a smaller profit potential and less incentive to cheat

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[415] CX 1681 C. *See* Hilke, Tr. 6030, 6033 (CX 1681 used Nielsen data for food stores in Bexar County, which includes San Antonio).

[416] *Id.*

[417] This situation contrasts sharply with that in County Lake Foods, Inc., in which the three largest distributors accounted for 90% of sales and the product involved -- milk -was not differentiated, so that distributors could credibly assert that a substantial increase in milk prices would prompt aggressive negotiations to seek a price reduction or an alternative supplier. *See Country Lake Foods*, 754 F. Supp. at 679 ("Fluid milk processors face no significant product differentiation barrier. Therefore, a food distributor could change its supplier of fluid milk without losing sales due to brand loyalty.").

[418] Davis, Tr. 4495-97, 4499-501.

[419] Bodnar, Tr. 1488-90.

[420] *See, e.g., Baker Hughes*, 908 F.2d at 986 (power buyers could decrease the likelihood of collusion where awards of lumpy orders -- sometimes exceeding $1 million -- were made through confidential bidding by sophisticated buyers).

[421] Davis, Tr. 4512-13.

than if promotions were contracted on a long-term basis.[422] In addition, changes to ad features and low-priced ad features would be quickly observable by other branded CSD bottlers, whose DSD delivery personnel can easily observe new promotions.[423]

2. The Ability to Induce New Entry or Vertically Integrate

There is no record evidence that any of the retailers in this market would vertically integrate into the production of branded CSDs in order to avoid payment of a collusive price increase. In order to do so, a retailer would need a branded CSD franchise for a product such as Coke or Pepsi or Big Red, and there is no evidence to show that a retailer could wrest those franchises away from their current holders.

Nor is there any evidence that retailers would induce new entry by another branded CSD bottler as a remedy to anticompetitive price increases. Indeed, as we discuss below, the evidence demonstrates that entry into the bottling of branded CSDs is extremely difficult, because of the difficulty of obtaining a branded CSD franchise and associated problems. Thus, we find that this case is not comparable to those in which power buyers could decrease the likelihood of collusion because they could induce new entry or vertically integrate themselves to avoid succumbing to a collusive price increase.[424]

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[422] Courts have noted that the possibility of a single large sale that is unlikely to be detected may tempt cheating by a cartel member. *E.g., FTC v. Elders Grain, Inc.*, 868 F.2d 901, 905 (7th Cir. 1989). It has also been noted that excess capacity can make it possible for a cartel cheater to supply a large quantity at little cost, thereby making the cartel cheating even more tempting. *Elders Grain*, 868 F.2d at 905-06.

In this case, the ALJ also found that the presence of excess capacity in this market reduced the likelihood of collusion. ID 74. We find that the existence of excess capacity in this particular market with its own set of distinctive market conditions would not significantly reduce the likelihood of collusion. If excess capacity were a major factor here, we would expect the record to show some pricing pressure effect from it; we have not seen any. In addition, product differentiation may mitigate the effect of excess capacity, since retailers would not necessarily find it profitable to substitute all of one branded CSD for sales of two others. *See* Section IV.C *supra*. In addition, we find the assertions of excess capacity to be somewhat inflated. Although the ALJ found that Grant-Lydick operates with 20-40% of unused capacity during the busiest time of the year, IDFF paragraph 134, the ALJ failed to note that this applies only to bottles, since Grant-Lydick contract packs its cans. Turner, Tr. 1117; Bodnar, Tr. 1526-27. The excess capacity listed for the Pepsi COBO -- IDFF paragraph 136 -- fails to note that sales of branded CSDs are highly seasonal, and that therefore excess capacity in February may be used capacity in July or December. Davis, Tr. 4513-14. Certain other citations to excess capacity involve bottlers that we have determined fall outside of the relevant market. *E.g.*, IDFF paragraph 135, 137, 138, 139. Thus, we are not convinced that there is a great deal of excess capacity in the relevant market in any case.

[423] *See* CX 465 A.

[424] *Cf*. *Country Lake Food, Inc.*, 754 F. Supp. at 679-80 (3 largest distributors had capability to vertically integrate, but court noted that possibility of vertical integration alone would not be sufficient to rebut presumption of market power).

3. Conduct by Retailers

Finally, we have examined whether conduct by any of the retailers suggests an ability to undermine a cartel among branded CSD bottlers. Although the evidence shows that H.E.B. and other large retailers have some bargaining power,[425] they do not add up to the type of conduct indicative of retailer's ability to turn to alternatives and thereby defeat a branded CSD bottler cartel. Indeed, the evidence is consistent that neither H.E.B. nor Kroger have attempted the type of market conduct that might indicate oligopsony power over branded CSD bottlers.[426]

In any case, even if H.E.B. as a retailer accounting for significant portions of the sales of CCSW and Pepsi COBO could defeat a collusive price increase from branded CSD bottlers, that action may only protect H.E.B., not other retailers. The discounts (including payments for ads and displays) negotiated between branded CSD bottlers and retailers are individualized, so the fact that H.E.B. continued to receive a competitive price would not necessarily protect other retailers from supracompetitive prices. That an anticompetitive effect may pertain only to some portion of the market does not immunize it from antitrust liability.[427]

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[425] For example, H.E.B. and Kroger each have cancelled scheduled ads because they determined that the price was not competitive. Summers, Tr. 6626-27; Kaiser, Tr. 3218. H.E.B., Kroger, and Albertson all require that bottlers offer them their lowest net wholesale price. Brinkley, Tr. 2234; Bodnar, Tr. 1660-61; Chapman, Tr. 7245; Turner, Tr. 1200; Summers, Tr. 6646, CX 3700-D; Donald, Tr. 5320-21, 5327-28; Kaiser, Tr. 3264. These events reflect the ability of the large retailers to ensure that they are getting prices that are comparable to those offered other retailers, but they do not show that the retailers could counteract a branded CSD bottler cartel.

[426] H.E.B. has never dictated the terms or conditions under which branded CSDs are sold in San Antonio or any other Texas market. Brinkley, Tr. 2235-36; Chapman, Tr. 7242; Gonzaba, Tr. 2100-01. Specifically, H.E.B. has never dictated or attempted to dictate package sizes or product lines, prohibited or attempted to prohibit any bottler from running a branded CSD advertisement with one of H.E.B.'s competitors, asked that a bottler stop selling a particular package size to an H.E.B. competitor, or used its advantage in one market to gain an advantage in another market. Brinkley, Tr. 2236-40; Chapman, Tr. 7242-44; Gonzaba, Tr. 2101-02.

Kroger has never dictated the terms and conditions under which branded CSDs may be sold in San Antonio or any other Texas market. Kaiser, Tr. 3215-16. Indeed, Kroger has threatened not to run ads unless they got an equal deal on price, but never got a better price than others. Kaiser, Tr. 3216.

[427] *See, e.g., United States v. United Tote*, 768 F. Supp. 1064 (D. Del. 1991) (liability found where 52% of market would be affected); *FTC v. Bass Bros. Enters.*, 1984-1 Trade Cas. (CCH) paragraph 66,041 at 68,605 (N.D. Ohio 1984) (liability found where less than 1/3 of industry would have been affected).

VII. ENTRY

We have held that a "primary consideration in evaluating the likely competitive effects of a merger or acquisition is the ease or difficulty with which new competitors might enter the market in response to supracompetitive pricing." Owens-Illinois, slip op. at 27-28. Under the Merger Guidelines, we recognize that if entry is "so easy that market participants, after the merger, could not profitably maintain a price increase above premerger levels," then the merger is unlikely to lead to the exercise of market power. Merger Guidelines, Section 3.0. In such circumstances, the absence of barriers to entry "makes it highly unlikely that a merger or acquisition will have anticompetitive effects, because any effort to extract supracompetitive prices and profits will induce new entry, which will reduce prices to competitive levels." *B.F. Goodrich*, 110 FTC at 295-96. On the other hand, "if prompt, effective entry is unlikely, customers may be exposed to sustained periods of anticompetitive harm." Owens-Illinois, slip op. at 28.[428]

In this case, the issue is whether a new bottler of branded CSDs could enter or whether an existing branded CSD bottler could expand sufficiently to remedy the anticompetitive effects that we have identified as likely from the acquisition at issue.[429] As we have recently noted, "[t]he Commission traditionally has assessed ease of entry by looking for identifiable barriers or impediments that could foreclose entry or prevent expansion by existing smaller firms sufficient to forestall anticompetitive conduct within the relevant market." Coca-Cola Co., Dkt. No. 9207, slip op. at 54. Entry barriers include "any condition that necessarily delays entry into a market for a significant period of time and thus allows market power to be exercised in the interim." *Echlin Mfg. Co.*, 105 FTC 410, 486 (1985). We have

[428] *See also United States v. Baker Hughes, Inc.*, 908 F.2d 981 (D.C. Cir. 1990); *United States v. Waste Management, Inc.*, 743 F.2d 976, 982 (2d Cir. 1984).

[429] Under Section 1.32 of the Merger Guidelines, certain firms that participate in the market through supply-side response are included as participants in the market, and are therefore treated separately from other firms that may enter the market. Here, following the Merger Guidelines avdroach would lead to the same conclusion.

We have found that expansion by CCUSA and DPUSA in sales of post-mix fountain syrup would be unlikely to prevent or disrupt tacit collusion by branded CSD bottlers. *See* Section VI.C.l. *supra*. We also find that the record does not show that CCUSA and/or DPUSA would be likely to enter into bottling in order to disrupt price increases by branded CSD bottlers; the long list of cases in which collusion by branded CSD bottlers was not prevented or disrupted by entry by CCUSA and/or DPUSA supports our conclusion on this issue. *See* Section VI.C.3 *supra*.

pointed out that "[b]arriers or impediments need not be absolute; rather, they are assessed 'in terms of the amount of time required for a motivated outsider to effect entry.'" Coca-Cola Co., slip op. at 54, *citing Olin Corp.*, 113 FTC at 612; Owens-Illinois, slip op. at 28.[430]

We find that the evidence in the record demonstrates that entry by a new branded CSD bottler would be difficult. The ALJ agreed. Although the ALJ found that entry "as a soft drink distributor is easy," he noted that, if the product and geographic markets asserted by complaint counsel were accepted, then entry barriers existed.[431] CCSW, the respondent, agrees. CCSW management has stated that "the bottling business is characterized by. . . high barriers to entry."[432] TBG, the owner of respondent, also agrees. A TBG presentation to its Credit Committee stated that TBG operates in an industry with "strong barriers to entry/franchise monopolies/few competitors."[433]

Some aspects of the soft drink bottling businesses do not present any obstacles to entry. We agree with the ALJ that the costs to lease delivery trucks and a warehouse are relatively small, and that a start-up distributor could purchase contract-packed bottled and canned soft drinks without any capital expenditures for equipment. IDFF paragraphs 378, 380. If we had included private label and warehouse-delivered CSDs in the relevant product market, we most likely would have agreed with the ALJ that entry into such a market would not be difficult.

But sales of branded CSDs are what concern us here, and entry as a branded CSD bottler is significantly more difficult. A branded CSD bottler must have a sufficient line of brands to be large enough to take advantage of various scale economies relating to the production, distribution, and marketing of CSDs. In Coca-Cola Co., we found that "[a] bottler needs at least 8% to 15% of the local market for carbonated soft drinks to achieve minimum efficient scale." Slip op. at 57. The record here indicates that even a higher market share -- perhaps over 20% where the bulk of the market is attributable to a single "flagship" brand -- may be necessary where one bottler such

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430 The Merger Guidelines use a comparable analysis, assessing entry as "easy" if it is "timely, likely, and sufficient in its magnitude, character, and scope to deter or counteract the competitive effects of concern." Section 3.0.

431 ID 72 & n.22; IDFF paragraph 396.

432 CX 1406 Z9.

433 CX 3806 I.

as CCSW dominates the market.[434] Conversely, branded CSD companies look to place their franchises with bottlers that have large enough operations that they can take advantage of such economies.[435]

Certain of the most important requirements for successful operation as a branded CSD bottler interact, creating a situation in which each element is necessary in order to obtain the others. For example, a branded CSD bottler must have a sufficient line of brands to generate enough volume to justify the costs of DSD delivery.[436] As we noted previously, the testimony is consistent that DSD delivery is critical for the success of a branded CSD bottling operation.[437] Conversely, in order to obtain a branded CSD franchise, a bottler would need to show that it intended to use DSD delivery.[438]

Moreover, to provide effective competition sufficient to thwart any unilateral or collusive anticompetitive activity, a new branded CSD bottler would need a line of brands with name recognition and volume sufficient to induce retailers to agree to ad features, not just in-store or other, less effective promotional activities.[439] As Mr. Kaiser of Kroger explained, in selecting a brand for an ad-buy program, "[t]he most important consideration we have is how strong the brand is [*i.e.*, name recognition] and how many cases we can sell of it [*i.e.*, volume]." Kaiser, Tr. 3231-32.

As this discussion of the evidence makes clear, a key to competitive effectiveness as a branded CSD bottler is to obtain a line of brands sufficient to generate volume that will support the use of DSD delivery and the achievement of minimum efficient scale, and a volume and market share sufficient to provide the name recognition and throughput necessary to "grow the brand" through ad features and other significant promotions. In particular, a "cola" is necessary

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[434] Both Mr. Bodnar and Mr. Turner testified that DP-SA had just reached critical mass in terms of ability to obtain ad features in 1983, when DP-SA had just reached a market share in food stores of 22.6%. CX 1681 C; *see also* Section VI.C.2.a *supra*.

[435] *See, e.g.*, Amicus Brief of DPUSA at 6-9

[436] CX 3941 at 288 [Schmid]; *see also* Sections IV.C.2, VI.C, D *supra*

[437] *See* Section IV.C.2, VI.C, D *supra*.

[438] *See* Section IV.C.2 *supra*.

[439] *See* Section VI.C.2 *supra* (Grant-Lydick has not provided significant competition to CCSW and Pepsi COBO where Grant-Lydick could not obtain ad features).

to generate such volume.[440] The fact that the branded CSD bottlers that obtain ad features are those whose concentrate companies invest millions of dollars in advertising for their brands also indicates that a brand backed by substantial advertising by its concentrate company is necessary to achieve a level of competitive effectiveness sufficient to prevent an anticompetitive price increase.[441]

But it would be very difficult for a new entrant to obtain such a brand, much less a line of such brands. As we observed in Coca-Cola Co., "[m]ost local markets for carbonated soft drinks have a Coca-Cola bottler, a Pepsi-Cola bottler, and a so-called 'third bottler,' which carries various brands of soft drinks other than Coca-Cola or Pepsi-Cola brands." Slip op. at 57.[442] The concentrate companies for branded CSDs are most interested in placing their brands with incumbents who have proven track records, not with new entrants who may or may not be able to reach minimum efficient scale.[443]

In light of these facts, it is not surprising that expansion by an incumbent branded CSD bottler to defeat an anticompetitive price increase would also be very difficult. The pattern of franchise transfers in the relevant market has been that branded CSD concentrate companies seek to move their franchises to the largest bottler that is not prohibited from having them due to flavor restrictions.[444] Just as DPUSA moved its franchise to CCSW, so Dr Pepper/7-Up moved the 7-Up franchise from Texas Bottlers -- with a 3.2% total branded market share in 1986[445] -- to Grant-Lydick, with approximately a 14.3% total branded market share in 1986.[446] This pattern reveals franchise moves that cause increasing concentration in this market,

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[440] Bodnar, Tr. 1253-54.

[441] *See* Section IV.C.3 *supra.*

[442] *See also* Lydick, Tr. 2937, 2943.

[443] *See* CX 3989 at 36 [Shanks].

[444] Bottling franchises prohibit a bottler from selling more than one brand in a "flavor segment." IDFF paragraph 105; CX 1668; RX 2938 C.

[445] CX 1681 D.

[446] *See* CX 1681 C (adjusting Grant-Lydick's 1986 market share in food stores of 16.8%, CX 1681 C, for fountain based on an interpolation of .85 from data in CX 4146 H results in an approximate market share of 14.3% for Grant-Lydick in 1986). When Grant-Lydick acquired 7-Up, 7-Up had a market share of about 3%. (*See* 3.8% share in food stores shown in CX 1681 D, adjusted for fountain by .23 factor set forth in CX 4146 H, results in overall market share of 2.9%) The addition of this market share still was not sufficient to enable Grant-Lydick to reach the critical mass that DPSA had just achieved in 1983 with the combination of Dr Pepper, RC, Canada Dry, and other branded CSD franchises. Bodnar, Tr. 1253-54.

not expansion that would defeat an anticompetitive price increase.[447] Accordingly, we find that expansion by an existing incumbent as well as entry by a new branded CSD bottler would be unlikely to defeat anticompetitive conduct in this market.[448]

VIII. THE SOFT DRINK INTERBRAND COMPETITION ACT

In a separate argument, respondent maintains that the Soft Drink Interbrand Competition Act ("SDICA"), 15 U.S.C. 3501-03, governs this proceeding and mandates dismissal of the complaint.[449] We disagree.

It is apparent from the very language of the SDICA that the statute is a narrow one that does no more than legalize exclusive territorial restrictions and transshipping prohibitions.[450] The SDICA is thus solely concerned with legitimizing these vertical non-price restraints; it does not address horizontal acquisitions, which remain exclusively within the purview of the existing antitrust laws. Because the present case involves a horizontal acquisition and in no way

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447 This pattern is consistent with a long-standing trend to bottler consolidation throughout the United States. *See* note 359 *supra.*

448 The Answering Brief of Respondent-Appellee did not assert any efficiencies that allegedly would outweigh any anticompetitive effects of the acquisition. Nonetheless, Respondent's Proposed Findings of Fact contain certain facts labelled as efficiencies. *See, e.g.*, RPFF paragraphs 527-531. To the extent that respondent relies on these facts on appeal, we find that such alleged efficiencies do not outweigh the likelihood of a substantial lessening of competition due to CCSW's acquisition of the Dr Pepper franchise, and that respondent made no showing that its alleged efficiencies could not be achieved by means other than the acquisition at issue in this case. *See* Merger Guidelines, Section 4.0.

449 The SDICA provides as follows, in pertinent part:

> Nothing contained in any antitrust law shall render unlawful the inclusion and enforcement in any trademark licensing contract or agreement, pursuant to which the licensee engages in the manufacture . . . , distribution, and sale of a trademarked soft drink product, of provisions granting the licensee the sole and exclusive right to manufacture, distribute and sell such product in a defined geographic area or limiting the licensee, directly or indirectly, to the manufacture, distribution, and sale of such product only for ultimate resale to consumers within a defined geographic area: Provided, that such product is in substantial and effective competition with other products of the same general class in the relevant market or markets.

15 U.S.C. Section 3501 (emphasis in original).

450 As the legislative history explains: "The Committee intends that [the SDICA] provide necessary relief [that is, legitimizing exclusive territorial agreements when not anticompetitive] without granting antitrust immunity and without establishing any precedent that would weaken our beleaguered antitrust laws." H.R. Rep. No. 96-1118, 96th Cong., 2d Sess. 2, 5 (1980) (emphasis added), reprinted in 1980 U.S.C.C.A.N. 2373, 2378. *See also Commonwealth of Pennsylvania v. Pepsico, Inc.*, 836 F.2d 173, 175-79 (3d Cir. 1988); *Pepsi-Cola Metropolitan Bottling Co. v. Checkers, Inc.*, 754 F.2d 10, 18 (1st Cir. 1985); *Coca-Cola Co. v. FTC*, 642 F.2d 1387, 1389-90 (D.C. Cir. 1981) (recognizing that the SDICA's sole purpose is to legitimize, under certain circumstances, the CSD industry's system of exclusive territorial distributorships).

challenges the existence of vertical territorial limitations and customer restraints,[451] the SDICA is completely inapplicable.

IX. APPROPRIATE RELIEF

Complaint counsel sought an order requiring divestiture of the Dr Pepper and Canada Dry franchises and prior approval by the Commission of any future acquisition by CCSW in the relevant market for a period of ten years from the date the Commission's order in this matter becomes final. The Commission has "wide discretion in its choice of a remedy," and "the courts will not interfere except where the remedy selected has no reasonable relation to the unlawful practices found to exist." *Jacob Siegel Co. v. FTC*, 327 U.S. 608, 61, 613 (1946). The Commission has the authority to impose prior approval requirements in merger cases. *Abex Corp. v. FTC,* 420 F. 2d 928 (6th Cir. 1970), *cert. denied*, 400 U.S. 865 (1970). *See also* Coca-Cola, slip op. at 63-64.

> [I]t is industry market structure and market conditions, not whether a 'knowing and deliberate violation' or a 'likelihood of repeated unlawful conduct' has been shown that determines the appropriateness of imposing a prior approval requirement in a particular case.

American Medical International, Inc., 104 FTC 1, 224 (1984).

We find that CCSW's acquisition of the Dr Pepper franchise in the San Antonio market is likely substantially to lessen competition among branded CSDs in that market, and we therefore order divestiture of the Dr Pepper franchise to a Commission-approved purchaser. Finding no anticompetitive effects from the acquisition of the Canada Dry franchise, we decline to order its divestiture.

In light of the highly concentrated market structure and the particular significance of increased market share in the branded CSD market in this case, we further order that CCSW must obtain Commission approval for any additional acquisitions in the relevant market for a period of ten years from the date on which the Commission's order in this matter becomes final.

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[451] In reaching this conclusion, we reject respondent's efforts to characterize the horizontal acquisition of assets (*e.g.* franchise agreements) from a competing bottler as a vertical transaction merely because licenses from concentrate companies are involved. If this argument were accepted, it would immunize virtually all acquisitions by bottlers, including the acquisition of a major competitor, from antitrust scrutiny.

STATEMENT OF COMMISSIONER DEBORAH K. OWEN, CONCURRING IN PART AND DISSENTING IN PART

I agree that the acquisition of the franchise to produce and distribute Dr Pepper by the Coca-Cola Bottling Company of the Southwest ("CCSW") was likely to substantially lessen competition in the San Antonio market for branded carbonated soft drinks ("CSDs"). I therefore concur in the order to divest this franchise and to require prior approval for certain future acquisitions. I must nevertheless dissent from some of the reasoning accompanying the opinion of two Commissioners, which speculates on issues neither presented to the Commission, nor necessary to a decision.

The record is replete with evidence indicating a strong presumption that this merger created or enhanced market power or facilitated its exercise in the San Antonio market for branded CSDs, accompanied by a strong anticompetitive effects story and difficult entry. The discussions in the opinion of two Commissioners relating to (1) the unilateral exercise of market power and (2) certain pricing behavior are, given the strength of the basic case, unnecessary to a just resolution of this matter, and therefore contrary to accepted notions of judicial construction.

CONCURRING STATEMENT OF COMMISSIONER DENNIS A. YAO

I concur with the opinion of the majority that branded CSDs are an antitrust product market. The record supports both this conclusion and the existence of strong product differentiation between the take-home and cold drink segments of that market. With respect to the latter point, Section IV.C.1 of the opinion discusses evidence that (i) Coca-Cola bottlers divide their businesses into take-home and cold drink markets, (ii) bottles/cans are handled and marketed very differently than fountain products, and (iii) substantial price differences exist between equivalent-sized take-home versus cold drink branded CSDs. Such evidence of differentiation suggests the possibility that take-home branded CSDs also comprise an antitrust product market. My deliberations in this matter have led me to question whether, in the face of a price increase by branded CSD bottlers, retailers (other than convenience stores) could substitute cold drink individual can or fountain cup sales for take-home sales in 3-liter PET bottles or 6-packs of 12-ounce cans, or whether fountain vendors could substitute sales in 3-liter PET bottles for individual can sales.[1] If we had found a smaller relevant antitrust product market (take-home sales of branded CSDs) within a larger one (branded CSDs) in this case, that would not have been unique.[2] A take-home branded CSD market in the San Antonio area would be even more concentrated than the branded CSD market that we found.[3] However, since neither com-

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[1] We had no need to consider this issue in Coca-Cola Co., Dkt. No. 9207 (June 28, 1994), where we were examining whether branded CSD bottlers could substitute concentrate or syrup for each other in the face of a price increase by a concentrate company. There, the evidence compelled the conclusion that branded CSDs were the smallest relevant product market, since concentrate and syrup are linked in that syrup can be manufactured from concentrate. Indeed, CCSW manufactures fountain syrup from concentrate. Summers, Tr. 6508-09.

[2] *See Olin Corp.*, 113 FTC 400, 598-600 (1990), *aff'd*, 986 F.2d 1295 (9th Cir. 1993), *cert. denied*, 114 S. Ct. 1051 (1994) (competitive effects analyzed within both a broader antitrust product market including the premium-priced and less expensive products, and a smaller antitrust product market consisting of only the premium-priced product).

[3] The pre- and post-acquisition HHIs would be:

Pre-acquisition HHI	3841
Post-acquisition HHI	4554
HHI Increase	713

CX 1681 A; Hilke, Tr. 6033. These HHIs are based on Nielsen data for soft drink sales in food stores in Bexar County (which includes San Antonio), comparing Oct./Nov. 1983 (pre-acquisition) with Aug./Sept. 1984 (post-acquisition) sales. Hilke, Tr. 6030. Since Nielsen data automatically exclude fountain and vending sales of branded CSDs, and since Bexar County accounts for 86% of the population in the 10-county relevant geographic market (Hilke, Tr. 6030, 6262; CX 4131 A), these data provide a reasonably accurate measure of take-home branded CSD sales in the San Antonio area.

plaint counsel nor respondent directly considered or briefed this possibility, we do not have a full record on which to decide this point, nor is it necessary, given the solid evidence of strong product differentiation within the branded CSD market.

FINAL ORDER

This matter having been heard on the appeal of complaint counsel from the initial decision, and on briefs and oral argument in support of, and in opposition, to the appeal; for the reasons stated in the attached opinion, the Commission has determined to grant the appeal in part, and reverse the initial decision. Accordingly,

It is ordered, That the following order be and the same hereby is ordered:

I. DEFINITIONS

It is ordered, That for the purposes of this order, the following definitions apply:

A. *"CCSW"* means Coca-Cola Bottling Company of the Southwest, its directors, officers, employees, agents and representatives, its successors and assigns, its predecessors, subsidiaries, divisions, groups and affiliates controlled by CCSW, directly or indirectly, and their respective directors, officers, employees, agents and representatives, and their respective successors and assigns.

B. *"Affiliate"* means any firm in which there is 10% or more ownership or control, directly or indirectly, between firms.

C. *"Concentrate"* means the base element, flavors or essences mixed according to a formula which, when added to carbonated water and nutritive or non-nutritive sweetener, is a carbonated soft drink.

D. *"Syrup"* means the concentrate and nutritive or non-nutritive sweetener which, when added to carbonated water, is a carbonated soft drink.

E. *"Carbonated soft drink"* means a carbonated beverage that does not contain alcohol and is produced by combining carbonated water with a sweetener and concentrates or with syrup.

F. *"Branded carbonated soft drink"* means a carbonated soft drink identified with any nationally or regionally recognized label,

name, or trademark that is, in general, heavily advertised, widely available, and ordinarily distributed by the direct-store-door delivery method. This definition does not include a label, name, or trademark associated solely with a single grocery or restaurant retailer, or with a generic flavor.

G. *"Branded concentrate or syrup"* means concentrate or syrup used to produce branded carbonated soft drinks.

H. *"Direct-store-door delivery"* means a method of distribution whereby the producer or distributor delivers product directly to the retail outlet and ordinarily positions the product for sale to the retailer's customers.

I. *"Acquired Dr Pepper assets"* means the franchise to produce and distribute Dr Pepper products acquired by CCSW from San Antonio Dr Pepper Bottling Company on or about September 1984 and any franchises to produce and distribute Dr Pepper products in the San Antonio area acquired by CCSW after September 1984.

II.

It is further ordered, That within twelve (12) months after the date this order becomes final, CCSW shall divest the acquired Dr Pepper assets absolutely and in good faith, at no minimum price. The divestiture shall be only to an acquirer, and only in a manner, that receives the prior approval of the Commission. Pending any divestiture required by this order, CCSW shall take all measures necessary to maintain the acquired Dr Pepper assets in their present condition and shall not cause or permit impairment of the marketability or viability of such assets. The purpose of the divestiture is to remedy the lessening of competition found in the Commission's decision.

III.

It is further ordered, That:

A. If CCSW has not divested the acquired Dr Pepper assets, absolutely and in good faith and with the Commission's prior approval, within twelve (12) months after the date this order becomes final, CCSW shall be subject to the appointment by the Commission of a trustee to effect the divestiture. In the event the Commission or the Attorney General brings an action pursuant to Section 5(1) of the

Federal Trade Commission Act, 15 U.S.C. 45(1), or any other statute enforced by the Commission, CCSW shall consent to the appointment of a trustee in such action. Neither the appointment of a trustee nor a Commission decision not to appoint a trustee under this paragraph shall preclude the Commission or the Attorney General from seeking civil penalties and any other relief available, including a court-appointed trustee, pursuant to Section 5(1) of the Federal Trade Commission Act, 15 U.S.C. 45(1), or any other statute enforced by the Commission, for any failure by the CCSW to comply with this order.

B. If a trustee is appointed by the Commission or a court pursuant to this order, CCSW shall be subject to or, in the case of a court-appointed trustee, shall consent to the following terms and conditions regarding the trustee's powers, authority, duties, and responsibilities:

(1) The trustee shall be selected and appointed by the Commission or, in the case of a court-appointed trustee, by the court. The trustee shall be a person with experience and expertise in acquisitions and divestitures. The appointment shall be effective fifteen (15) days (the "effective date") after CCSW's receipt of written notifications of such appointment or, in the case of a court-appointed trustee, at such time as the court may order, unless CCSW has, on or before the effective date, presented substantial grounds for disqualification of the trustee. In the event of such objection to the appointment of the trustee, the effective date shall be stayed pending a determination by the Commission or, in the case of a court-appointed trustee, by the court.

(2) The trustee shall have the exclusive power and authority, subject to the prior approval of the Commission, to divest the acquired Dr Pepper assets. The trustee shall have twelve (12) months from the date of appointment to accomplish the divestiture. If, however, at the end of the twelve-month period, the trustee has submitted a plan of divestiture or believes that divestiture can be accomplished within a reasonable time, the divestiture period may be extended by the Commission or, in the case of a court-appointed trustee, by the court.

(3) The trustee shall have full and complete access to the personnel, books, records and facilities of CCSW concerning the acquired assets, and CCSW shall develop such financial or other

information relevant to the property to be divested as the trustee may reasonably request. CCSW shall cooperate with the trustee, and shall take no action to interfere with or impede the trustee's accomplishment of the divestiture. Any delays in divestiture caused by CCSW shall extend the time for divestiture in an amount equal to the delay, as determined by the Commission or, for a court-appointed trustee, by the court.

(4) Subject to CCSW's absolute and unconditional obligation to divest at no minimum price and to the purpose of the divestiture as stated in paragraph II of this order, the trustee shall use his or her best efforts to negotiate the most favorable price and terms available in each contract that is submitted to the Commission for approval. The divestiture shall be made in the manner set out in paragraph II, provided, however, that if the trustee receives bona fide offers from more than one prospective acquirer, and if the Commission approves more than one such acquirer, then the trustee shall divest to the acquirer selected by CCSW from among those approved by the Commission.

(5) The trustee shall serve, without bond or other security, at the cost and expense of CCSW on such reasonable and customary terms and conditions as the Commission or a court may set. The trustee shall have the authority to employ, at the cost and expense of CCSW, such consultants, attorneys, investment bankers, business brokers, accountants, appraisers, and other representatives and assistants as are reasonably necessary to carry out the trustee's duties and responsibilities. The trustee shall account for all monies derived from the divestiture and for all expenses incurred. After approval by the Commission and, in the case of a court-appointed trustee, by the court of the account of the trustee (including fees for his or her services), all remaining monies shall be paid at the direction of CCSW, and the trustee's power shall be terminated. The trustee's compensation shall be based at least in significant part on a commission arrangement contingent on the trustee's divesting the acquired assets. CCSW shall indemnify the trustee and hold the trustee harmless against any losses, claims, damages, or liabilities arising in any manner out of, or in connection with, the trustee's duties under this order. Within forty-five (45) days after the appointment of the trustee and subject to the prior approval of the Commission and, in the case of a court-appointed trustee, of the court, CCSW shall execute a trust agreement that transfers to the

trustee all rights and powers necessary to permit the trustee to effect the divestiture required by this order.

(6) If the trustee ceases to act or fails to act diligently, a substitute trustee shall be appointed in the same manner as provided in this paragraph.

(7) The Commission (or, in the case of a court-appointed trustee, the court) may on its own initiative or at the request of the trustee issue such additional orders or directions as may be necessary or appropriate to accomplish the divestiture required by this order.

(8) The trustee shall report in writing to CCSW and to the Commission every sixty (60) days concerning his or her efforts to accomplish divestiture.

IV.

It is further ordered, That, within sixty (60) days after the date this order becomes final and every sixty (60) days thereafter until CCSW has fully complied with the provisions of paragraphs II and III of this order, CCSW shall submit to the Commission a verified written report setting forth in detail the manner and form in which it intends to comply, is complying or has complied with those provisions. CCSW shall include in its compliance reports, among other things that are required from time to time, a full description of all substantive contacts or negotiations for the divestiture of the acquired Dr Pepper assets, including the identity of all parties that either contacted CCSW or were contacted by CCSW. CCSW also shall include in its compliance reports copies of all written communications to and from such parties, all internal memoranda, and all reports and recommendations concerning divestiture.

V.

It is further ordered, That CCSW, for a period of ten (10) years from the date this order becomes final, shall not acquire, directly or indirectly, without the prior approval of the Commission:

A. The whole or any part of the stock, share capital, or equity interests in any company or firm:

(1) Engaged in the manufacture, distribution, or sale of branded concentrate or syrup or branded carbonated soft drinks; ~~or~~

(2) Engaged in the franchising or licensing of any brand, name or trademark used in connection with the manufacture, distribution, or sale of branded concentrate or syrup or branded carbonated soft drinks; or

(3) Holding an exclusive franchise or license of any branded concentrate company

in any geographic area in which CCSW is engaged in the manufacture, distribution, or sale of branded concentrate or syrup or branded carbonated soft drinks; or

B. Any franchise, license, brand, label, name or trademark associated with, or any assets engaged in, used for, or previously used for (and still suitable for) the manufacture, distribution, or sale of concentrate, syrup or carbonated soft drinks in any geographic area in which CCSW is engaged in the manufacture, distribution, or sale of branded concentrate or syrup or branded carbonated soft drinks. Provided, however, that this provision shall not apply to the purchase or acquisition of any assets worth less than $100,000.

One (1) year after the date this order becomes final, and annually thereafter for the following nine (9) years and at such other times as the Commission or its staff may request, CCSW shall file with the Commission a verified written report of its compliance with paragraph V of this order.

VI.

It is further ordered, That, for the purpose of determining or securing compliance with this order, and subject to any legally recognized privilege, upon written request and on reasonable notice to CCSW made to its principal office, CCSW shall permit any duly authorized representatives of the Commission: (A) access, during office hours and in the presence of counsel, to inspect and copy all books, ledgers, accounts, correspondence, memoranda and other documents in the possession or under the control of CCSW relating to any matters contained in this order; and (B) upon five (5) days notice to CCSW and without restraint or interference from CCSW, to interview officers or employees of CCSW, who may have counsel present, regarding such matters.

VII.

It is further ordered, That CCSW shall notify the Commission at least thirty (30) days prior to any proposed change in CCSW such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation, dissolution or sale of subsidiaries or any other change that may affect compliance obligations arising out of the order.

Commissioner Azcuenaga and Commissioner Starek recused.[1]

[1] Prior to leaving the Commission, former Commissioner Owen registered her vote in the affirmative for the Opinion of the Commission and the Final Order in this matter, with the notation that she dissented in part, as to discussions in the Opinion of the Commission relating to the unilateral exercise of market power and certain pricing behavior.