



US proposes new Horizontal Merger Guidelines

The US antitrust enforcement agencies recently released proposed new Horizontal Merger Guidelines. The proposed Guidelines demonstrate the agencies' movement away from the traditional linear framework for merger analysis – embodied in the previous 1992 version of the Guidelines – to a more holistic, multi-factor and fact-specific approach. The proposed Guidelines and their effect on merger review analysis in the US are explored in detail below.

Modern merger review practice underwent an important change with the publication of new proposed Horizontal Merger Guidelines (proposed Guidelines) by the United States Federal Trade Commission (FTC) and Antitrust Division of the Department of Justice (DOJ) (collectively, the Agencies),¹ designed to more accurately reflect current standards and practices at the Agencies.

The previous Guidelines were untouched since 1992, with the exception of 1997 revisions to the efficiencies section. The 1992 Guidelines have been criticised for a rigid and dogmatic portrayal of the investigative techniques and substantive standards employed by the Agencies. The proposed Guidelines provide lengthy and detailed insights into the wide array of factors that influence an Agency's determination as to whether a horizontal merger may substantially lessen competition and should therefore be challenged. In broadest strokes, the draft memorialises current practice as it has evolved over the last 18 years and the proposed Guidelines reflect a reworking of the 1992 Guidelines in style, tone and often in substance.

The proposed Guidelines admit that there is no uniform application of a single methodology and demonstrate that many factors can influence an Agency enforcement decision. The proposed Guidelines will provide the Agencies with greater flexibility to define a competitive problem, with the proposed Guidelines as their intellectual guidepost.

In addition, the proposed Guidelines provide an important opportunity for the Agencies to try to

educate the judiciary regarding their views of merger enforcement. In recent years, a sceptical judiciary has frowned upon attempts by the Agencies to move away from the letter of the 1992 Guidelines.

The revisions may help sway the courts but – given the existing precedent – the influence of these proposed Guidelines on the courts will take time to assess.

Parties contemplating transactions should be aware of these myriad factors and the often complicated relationship between them, in order to ensure their interests are adequately represented before the FTC and DOJ.

An end to the linear approach

The 1992 Guidelines described a mechanical five-step linear process to assess whether a challenge to a horizontal merger was appropriate. The proposed Guidelines depart from this linear exposition and instead embrace a malleable fact-intensive approach, with a focus on a broad range of analytical tools to determine whether a merger challenge is appropriate.

The Agencies' analytical toolkit

The Agencies' toolkit is substantial yet the proposed Guidelines make clear that no particular tool will prove dispositive to a merger challenge. Rather, the reviewing Agency will approach each transaction holistically and make a determination as to which tools will enhance their investigation.

¹ The full text is available online at www.ftc.gov/os/2010/04/100420hmg.pdf.

The proposed Guidelines provide a new and prominent section on types of evidence the Agencies will consider, including:

- the actual effects in consummated mergers;
- a thorough review of ‘natural experiments’ where analogous events occurred;
- an analysis of market shares and concentration, retaining use of the Herfindahl-Hirschman Index (HHI) measure of concentration, albeit at different thresholds (see the table entitled ‘Revised HHI guides’ at the end of this briefing);
- a review of the extent of head-to-head competition between the parties; and
- whether one of the merging parties is a ‘maverick’ firm that plays a key disruptive role in the market through, for example, aggressive pricing, a new technology or business model, to the benefit of consumers.

The Agencies will continue to gather evidence from the merging parties with an emphasis on, and preference for, ordinary course documents rather than documents created during the pendency of a merger review.

Views of customers and other industry participants will continue to hold sway but the Agencies will show appropriate scepticism to the views of rival firms.

In addition, the proposed Guidelines make clear that the Agencies will not shy from examining whether the effects of a potential transaction will impact differently-situated customers differently. Where price discrimination in such markets is deemed feasible, the Agencies will evaluate the competitive effects separately by customer. Accordingly, the drawing of narrow product market definitions will not be exceptional.

Explaining the Agencies’ methodologies

Although the proposed Guidelines repeat many of the methodologies addressed in the 1992 Guidelines, the new document makes clear that a merger review is very much a complete analysis of all factors and not merely a series of rote steps. There is an explicit refutation of product market definition and geographic market definition as ends in themselves, or even as necessary starting points for the Agencies’ analysis. Instead, market definition is but one tool.

Importantly, several mainstays from the 1992 Guidelines reappear, including the following.

- The *hypothetical monopolist test* remains in force as a method to ascertain whether a small but significant and non-transitory increase in price (SSNIP) would shift sales such that a group of products should be considered as a single product market (or not).
- The possibilities of *entry* remain an important consideration in defining the competitive effects of a given transaction. Where entry is timely, likely, and sufficient, an otherwise anticompetitive transaction may not face a challenge. The Agencies have moved away from a two-year timeliness requirement and instead now require that entry be ‘rapid.’
- *Efficiencies* will continue to be credited in assessing a transaction, so long as the efficiencies are merger-specific, concrete, non-speculative and verifiable by reasonable means.

Some of the most notable changes are as follows.

- An expanded discussion of *unilateral effects and product market definition*. Generally, the document embodies a number of the economic concepts that have been developed over the last 10-15 years. There is an explicit reference to use of diversion ratios in merger analysis (ie, quantifying the extent of direct competition between the merging firms by estimating the fraction of unit sales lost by one firm’s product – and transferred to the other party’s product – due to an increase in price), and an embrace of economic principles reflecting ‘upward pricing pressure’. Bargaining and auction markets are addressed separately with the Agencies, revealing their perspective that where, prior to the transaction, the merging parties had been each other’s most common competitor, the likelihood of anticompetitive effects resulting from the transaction is greater. This discussion also makes quite clear that the competitive relationship between the products of the merging parties is far more important than market definition or shares. In addition, if a proposed transaction will decrease innovation between firms once competing on such a basis, the Agencies may be led to conclude that anticompetitive effects are possible. Finally, the proposed Guidelines abandon the previous (and often misunderstood) reference to a 35 per cent market share safe harbour. Especially with regard to

unilateral effects, but across all topics, the proposed Guidelines mirror many of the findings reflected in the Agencies' 2006 Horizontal Commentary on the Merger Guidelines.

- A reworked *co-ordinated effects* section that makes clearer that market concentration plays a far more important role under this theory of harm than in a unilateral effects case. In rough terms, markets will be deemed 'vulnerable to co-ordinated conduct' based on factors such as those shown in the table entitled 'Evidence a market is vulnerable to co-ordinated conduct', at the end of this briefing.
- A new, separate section on *power buyers*, conveying that power buyers are often not a complete 'defence' or a panacea for otherwise potentially anticompetitive effects.
- A new section on *mergers of competing buyers*, setting out established principles regarding the creation of monopsony power, which has formed the basis of a number of enforcement actions over the years.
- A new section on *partial acquisitions*, articulating the three general principles of reduced competitive incentives; increased risk of co-ordination; and flow of sensitive information, that the Agencies have used to challenge minority investments or holdings in competitors.

Next steps

The proposed Guidelines represent seven months of study, dialogue during a number of public hearings, and the review of numerous public comments. Additional public comments will be accepted until 20 May 2010, with publication of the final version anticipated in the next several months. While some edits following the public comment period are inevitable, it is highly likely the final version will reflect the same priorities and preferences embodied in the proposed Guidelines; substantial changes seem unlikely.

Revised HHI guides

Market	Post-merger HHI	HHI Δ	Standard
Unconcentrated	<1500	Any	Unlikely to have adverse competitive effects and ordinarily require no further analysis.
Moderately concentrated	1500-2500	>100	Potentially raise significant competitive concerns and often warrant scrutiny.
Highly concentrated	>2500	100-200	Potentially raise significant competitive concerns and often warrant scrutiny.
	>2500	>200	Presumed to be likely to enhance market power. The presumption may be rebutted by persuasive evidence showing that the merger is unlikely to enhance market power.

Evidence a market is vulnerable to co-ordinated conduct

Factors that the Agencies will consider include:

- previous express collusion;
- transparency of competitive initiatives, including terms of dealing;
- product homogeneity;
- size and frequency of sales or contracts;
- market elasticity of demand; and
- buyer size and characteristics.

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