

# Weil Briefing: Antitrust/Competition

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## FTC and DOJ Issue New Horizontal Merger Guidelines

On August 19, 2010, the U.S. Federal Trade Commission (“FTC”) and the U.S. Department of Justice, Antitrust Division (“DOJ”) jointly issued new Horizontal Merger Guidelines (“2010 Guidelines”). These guidelines replace the Horizontal Merger Guidelines that were originally issued by the two agencies in 1992 and slightly revised in 1997 (“1992 Guidelines”).

Prior to issuing the 2010 Guidelines, the FTC and DOJ held multiple public workshops, and received public comments from attorneys, academics, consumer groups, and other interested parties. In addition, in April 2010, the agencies circulated a proposed version of the guidelines for public comments. The agencies have incorporated input from the workshops and comments into the final 2010 Guidelines.

According to FTC Chairman Jon Leibowitz, the 2010 Guidelines “provide a clearer and more accurate explanation to merging parties, courts, and antitrust practitioners of how the agencies review transactions.” DOJ Assistant Attorney General Christine Varney stated that the 2010 Guidelines “better reflect the agencies’ actual practices, ... provide more clarity and transparency, and will provide businesses with an even greater understanding of how [the agencies] review transactions.” Although supporting issuance of the 2010 Guidelines, Commissioner Rosch lamented that, in his view, the guidelines overemphasize economic models and price theories, and fail to sufficiently address effects on non-price competition.

In brief, the 2010 Guidelines: focus on competitive effects of a merger, while de-emphasizing the importance of market definition to the agencies’ analysis; explain the analytical tools and methodologies that the agencies will use for merger analysis; identify the categories of evidence that may be considered as part of the analysis; and increase the extent to which economic analysis will be used as part of the process for assessing potential competitive effects. The agencies emphasize that the merger review process will be flexible and fact-specific.

Bottom line: The 2010 Guidelines appear to provide the agencies with more tools, especially economic ones, to potentially challenge mergers. As a result, compared to the agencies’ earlier merger guidelines, the 2010 Guidelines offer less predictability regarding which analytical methodology will be applied and the likely outcome of an investigation. In addition, although the 2010 Guidelines are intended to reflect the current state of the agencies’ merger review policy and procedures, the language and tone of the 2010 Guidelines suggest that the agencies may challenge a greater number of transactions than in the past.

### **The 2010 Changes**

The 2010 Guidelines include several major changes from the 1992 Guidelines as well as a number of other important modifications and clarifications.

- The 2010 Guidelines state that market definition will no longer be the necessary first step of the merger analysis. Instead, the agencies will use market definition to: specify the line of

commerce and section of the country in which competitive concerns may arise; and identify market participants and measure market share to the extent the measurements illuminate the competitive effects of a horizontal merger. Market definition principles also will be used to analyze the substitutes available to customers. Although the agencies normally will identify relevant markets, they may conclude that a merger raises competitive concerns without defining a precise relevant market if there is evidence that the merger likely will result in anticompetitive effects.

- The primary market definition principle used to assess the parameters of a relevant market will continue to be the hypothetical monopolist test (i.e., whether a hypothetical monopolist profitably could impose a small but significant and non-transitory increase in price (“SSNIP”). Most often the hypothetical SSNIP used will be a five percent price increase, although it could be higher or lower depending on the industry.
- In implementing the hypothetical monopolist test, the agencies will evaluate the firm’s incentive to raise prices, which depends both on the extent that customers would turn to substitutes and the firm’s profit margins. Accordingly, the agencies will assess the merging firms’ incremental costs based on the companies’ documents and data, and if the necessary data are available, may consider economic “critical loss analysis” to corroborate inferences drawn from other sources of evidence. In addition, the agencies more explicitly will consider the closeness of competition among potential substitutes as part of the analysis at this stage, which could result in narrower market definitions where there are differentiated products or the potential for price discrimination.
- The 2010 Guidelines increase the Herfindahl-Hirschman Index (“HHI”) thresholds that the agencies use to evaluate a merger’s effect on market concentration:

2010 Guidelines Presumption	1992 Guidelines Presumption
<b>Change in HHI of less than 100 points</b> – unlikely to have adverse competitive effects, and ordinarily requires no further analysis	No similar standalone presumption
<b>Post-merger HHI below 1,500</b> (unconcentrated market) – unlikely to have adverse competitive effects, and ordinarily requires no further analysis	The unconcentrated market presumption applies to post-merger HHI of below 1,000
<b>Post-merger HHI between 1,500 and 2,500 and increase in HHI of over 100 points</b> (moderately concentrated market) – potentially raise significant competitive concerns and often warrant scrutiny	The moderately concentrated market presumption applies to post-merger HHI of between 1,000 and 1,800 and increase in HHI of over 100 points
<b>Post-merger HHI over 2,500 and increase in HHI between 100 and 200 points</b> (highly concentrated market) – potentially raise significant competitive concerns and often warrant scrutiny	The highly concentrated market presumption applies to post-merger HHI of over 1,800 and increase in HHI of between 50 and 100 points
<b>Post-merger HHI over 2,500 and increase in HHI of over 200 points</b> – rebuttable presumption that the merger likely will enhance market power	The enhanced market power presumption applies to post-merger HHI of over 1,800 and increase in HHI of over 100 points

- The agencies note, however, that the HHI thresholds will not be applied as rigid screens and that other competitive factors will be examined to determine whether increased concentration at any level will lead to adverse competitive effects.
- The 2010 Guidelines strongly emphasize the use of economic analysis as an integral part of merger review. The 2010 Guidelines describe a number of different economic analyses that the agencies may implement to help predict a merger's competitive effects, including diversion ratios, critical loss analysis, and merger simulation models.
- The 2010 Guidelines also provide:
  - Guidance that merger review policy prohibits transactions that “create, enhance or entrench market power or facilitate its exercise.” Framed in the overview section as an overall unifying theme of the 2010 Guidelines, this statement highlights that when a merging company already has a substantial market position, a transaction involving even a small competitor is likely to face close scrutiny.
  - Recognition that merger analysis is a highly fact-specific process, and accordingly, the agencies will not be confined to employing a single analytical methodology.
  - A discussion of the categories and sources of evidence that the agencies will use to predict a merger's competitive effects, including: the merging companies' documents, testimony, data, and explicit and implicit business decisions; product price levels and incremental costs; customers' views about the available substitutes and concerns about potential competitive effects; the transaction purchase price; and industry participants' assessment of the marketplace.
  - A significantly expanded discussion of the unilateral competitive effects theory, including: markets with differentiated products or the potential for price discrimination; markets where auctions or significant bargaining take place; output suppression incentives in markets for homogeneous products; and potential curtailment of innovation, elimination of products, or acquisition of a potential competitor.
  - A revised section on coordinated interaction and the coordinated effects theory, including factors that indicate that a market may be vulnerable to coordinated conduct, and theories of potential harm from coordinated conduct. The agencies also note that coordinated effects can include concerns about conduct that is not otherwise condemned by the antitrust laws.
  - A new section on the impact of powerful buyers on merger analysis, including a recognition that such buyers may help constrain competitive effects. However, the agencies also note that a merger still may enhance market power to the detriment of power buyers or other customers.
  - An explanation of how the agencies will examine whether entry into the market by one or more firms is so easy that it would be likely, timely and sufficient to alleviate concerns about potential competitive effects. However, there is no longer a specific time frame in which entry would be found timely.
  - A continued recognition that merger-specific efficiencies can enhance competition, and a reiteration that efficiencies will be weighed against potential adverse competitive effects so long as they are cognizable, substantiated and reasonably verifiable. The agencies note that when evaluating efficiencies claims in innovation markets, the agencies will credit

efficiencies that spur innovation, even where the efficiencies do not affect the merged firm's short-term pricing.

- Confirmation that the agencies apply a very high bar to successful application of a “failing firm” or “failing division” claim.
- A new section on mergers between competing buyers that can enhance buyer market power (also called “monopsony power”). The section notes the importance of distinguishing a reduction in prices paid by the merged firm due to enhanced buyer power from price reductions due to procompetitive merger efficiencies.
- A new section on how the agencies will evaluate acquisitions of partial interests in competing firms. The agencies will focus on whether the acquisition: gives the acquirer the ability to influence the target's competitive conduct; reduces the acquiring firm's incentives to compete; or gives the acquirer access to the target's competitively sensitive information.

### **Potential Ramifications**

The 2010 Guidelines are a very important development in US merger review policy. The revised guidelines were anticipated and many of the analytical tools and methodologies already were used by some FTC and DOJ staff. However, the 2010 Guidelines raise a number of important issues for merging firms:

- The 2010 Guidelines emphasize the agencies' focus on the bottom line of predicting a merger's likely competitive effect, and broaden the analytical tools the agencies can employ to reach or support predictions regarding competitive effects.
- Because the 2010 Guidelines emphasize the use of economic analyses, merging companies could receive broad data requests from the agencies, and companies should be prepared to address the agencies' expanded legal and economic arguments, including affirmatively developing econometric analyses.
- Although the HHI thresholds are increased, the revised treatment of market definition principles may result in narrower relevant markets, and therefore, higher concentration levels.
- The 2010 Guidelines detail the diverse types of evidence that the agencies may use to predict competitive effects, including numerous categories of the merging parties' documents, data and business conduct as well as information from customers and industry participants, all of which could result in longer investigations and broader requests for documents and information.
- To the extent that courts look to the 2010 Guidelines for direction in analyzing mergers, the new structure may make it easier for the FTC and DOJ to make their case given that the 2010 Guidelines provide a significantly expanded exposition of the information and theories that the agencies consider appropriate. However, it is unclear how courts will square the agencies' conclusions based on the 2010 Guidelines' analytical methodologies with the well-developed merger case law.
- The 2010 Guidelines' listing of the many and varied tools and methods available to the agencies provides practitioners with the knowledge of what tools and methods to bring to bear in merger analysis and presentations to the agencies. However, the 2010 Guidelines provide little guidance on what results from the various analyses are likely to be persuasive or

dispositive in the agencies' decisions whether to permit or seek to enjoin a transaction. In that sense, the 2010 Guidelines provides few true guidelines to assist parties considering a transaction.

Although the 2010 Guidelines are intended to reflect the current state of the agencies' merger review policy and procedures, the language and tone of the 2010 Guidelines suggest that the agencies may challenge a greater number of transactions than in the past.

The FTC's press release, statements by Chairman Leibowitz and Commissioner Rosch, as well as the 2010 Guidelines are available on the FTC website at:

<http://www.ftc.gov/opa/2010/08/hmg.shtm>

<http://www.ftc.gov/os/2010/08/100819hmg.pdf>

The DOJ's press release and the 2010 Guidelines are available on the DOJ's website at:

[http://www.justice.gov/atr/public/press\\_releases/2010/261642.pdf](http://www.justice.gov/atr/public/press_releases/2010/261642.pdf)

<http://www.justice.gov/atr/public/guidelines/hmg-2010.pdf>

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