Final Review

Merger Antitrust Law

Georgetown University Law Center

Dale Collins

Forms of Exam Questions: Some Examples
(not exhaustive)

Advising a Judge

- You are a law clerk to a judge
- For a given set of facts found by the judge in a bench trial for injunctive relief, write a memorandum—
  - Applying the law to these facts
  - Determining whether the plaintiff is entitled to relief
  - Recommending, if you conclude that the plaintiff is entitled to relief, what permanent injunctive relief should be entered

Advising the AAG

- You are a special assistant to the Assistant Attorney General in charge of the Antitrust Division[1]
- For a given fact situation—
  - Identify what claims the Division could bring
  - Evaluate the strength of the prima facie case
  - Evaluate the strength of the parties' defenses
  - Assess the likelihood of success on the merits in litigation
  - Make a recommendation whether the Division, as a matter of prosecutorial discretion, should pursue litigation
  - If you recommend litigation—
    - Recommend what relief the Division should seek in a fully litigated permanent injunction
    - Recommend whether the Division should accept lesser relief in a consent settlement

[1] this works equally well for a attorney-advisor to a FTC Commissioner or trial attorney writing for her section chief.

Advising a Partner (I)

- You are an associate in a law firm
  - You and a partner has just met with a new firm client seeking legal advice about an offer to be acquired that it has just received
  - The client is not knowledgeable about antitrust law and wants to better understand the antitrust landscape and your advice as to how to move forward in the negotiations of the purchase agreement
  - The client has provided you with some basic information about the industry, the parties to the transaction, and perhaps other things relevant to the transaction
- The partner has asked you to prepare a memorandum to send to the client addressing—
  - What standard the law applies to determine whether the transaction poses an antitrust problem
  - Whether the federal antitrust agencies are likely to review the acquisition and the process it would use if it did
  - What the likely outcome of the investigation is likely to be
  - What, if anything, the company can do in the negotiation of the purchase agreement to minimize the risk that the deal will be blocked

Advising a Partner (II)

- You are an associate in a law firm
  - You and a partner has just met with a new firm client seeking legal advice about a possible transaction
- The partner has asked you to prepare a memorandum addressing—
  - The merits
    - Spotting any theories of anticompetitive harm that might apply to the transaction
    - Developing the lines of any possible defenses for each theory
    - Identifying what facts, documents, and economic analysis should be pursued to assess the strength of the theories of anticompetitive harm and the possible defenses
  - The relief
    - Identifying what remedies might be demanded in the "reasonable worst case"
  - The strategy
    - Assessing who, if anyone, might have the ability and incentive to challenge the transaction (including whether the transaction is HSR reportable)
    - Suggesting a strategy for maximizing the support and minimizing the opposition to the transaction
    - Suggesting what provisions the client should seek to include in the purchase agreement (and what provisions the other side is likely to seek)

The Frozen Dinners Merger

Some initial observations

- Mergers arise in factually involved settings
- *Do not* become overwhelmed by the facts
- Read the problem once (or twice) to make sure you understand key questions

Some initial observations

- If asked to evaluate a case or assess antitrust risk, keep in mind the basic framework for a formal analysis:
  - Prima facie case
    - Product market definition
    - Geographic market definition
    - The *PNB* presumption
    - Supporting theories of anticompetitive harm
      - Unilateral effects
      - Coordinated effects
      - Elimination of a maverick
      - Exclusionary effects
  - Defenses
    - Entry/expansion/repositioning
    - Efficiencies
    - Countervailing buyer power
    - Failing company/division
  - Conclusion on legality (balancing)
  - Weighing of the equities (if appropriate)
  - Relief

Quick read

- What are you being ask to do?
  - Provide a preliminary antitrust risk analysis on the facts you have been given by Long
  - Identify the most important pieces of evidence that need to be developed in order to better assess the antitrust risk.

Quick read

- What are you initial impressions?
  - Two low calorie single serve frozen dinners firms are going to merge
  - Only three meaningful LC competitors
  - IF low calorie frozen dinners are a market, this is a 3→2 deal
    - Should easily trigger *PNB* presumption
    - Probably strong unilateral effects
    - Probably strong coordinated effects
    - No indication of a maverick
    - Maybe some exclusionary effects (shelf space)
  - Efficiency defense (?)
    - Usual fixed cost savings—not cognizable
    - But also some marginal cost savings in procurement
  - Entry defense (?)
    - Bellisio Foods
  - Deal probably is not fixable

Analysis/Outline

- The deal and the "market"
  - Intelligent Ones (IO) (#3 with 19.2%) considering acquisition by ConAgra (#2 with 22.1%) in low-calorie, single serve frozen foods
  - One other player—Nestle (#1 with 54.8%)
- *Key question*: Is low calorie single serve frozen foods a relevant product market?

Relevant product market

- Is low calorie single serve frozen foods a relevant product market?
  - Given diversion ratios
  - Try uniform SSNIP test on all low calorie frozen dinners
    - %Critical loss:

$$\%CL = \frac{\delta}{\delta + m} = \frac{0.05}{0.05 + 0.3} = 14.2\%$$

    - %Actual loss: 16.8%
    - FAILS

Relevant product market

- Is low calorie single serve frozen foods a relevant product market?
  - BUT these are differentiated products: TRY aggregate diversion ratio test
    - %Critical recapture rate =14.2%
    - %Actual recapture
      - IO → all other low calorie: 50%
      - Other low calorie → all other low calorie: 90%
      - [Other low calorie → IO: 0% -- DOES NOT MATTER: Look to the diversion into the candidate market, not the diversion to a particular product in the market]
    - PASSES

Relevant product market

- Is low calorie single serve frozen foods a relevant product market?
  - TRY 1-product SSNIP: Two possibilities—
    - Raise IO price—Good possibility, since 50% recapture in low calorie frozen foods
    - Raise Healthy Choice price—Unlikely, since zero percent recapture in low calorie frozen foods
  - BRUTE FORCE CALCULATION for IO PRICE INCREASE

DATA		
%SSNIP	5.0%	
IO price	$2.29	Table 2
IO total sales	$50,000,000	Table 1, 4
IO total units	21,834,061	Calculated
IO actual loss	16.6%	Table 3
Other LC recapture	50.0%	Table 3
%Margin (IO)	30%	Table 2
$margin (IO)	$0.69	Table 2
$margin (other LC)	$0.56	Table 2

CALCULATION	IO	
$SSNIP ($\Delta$p)	$0.1145	SSNIP * price
Retained units	18,209,607	(1-16.6%)*units
Gross gain	$2,085,000	
Lost units	-3,624,454	16.6% * units
$margin (m)	$0.69	
Gross loss	-$2,490,000	
Recapture rate	50%	
Margin on recap	$0.56	
Recapture sales	1,812,227	50% * lost units
Recapture gain	$1,014,847	
TOTAL GAIN	$609,847	
	PASSES	

Relevant product market

- Judicial tests
  - *Brown Shoe* "outer boundaries"
    - High diversion ratio (50%) from IO other low calorie frozen dinners
    - High diversion ratio (90%) from Lean Cuisine to Healthy Choice
    - High diversion ratio (90%) from Healthy choice to Lean Cuisine

Keep in mind:
1. You are looking for the most appropriate market in which to analyze a IO/Healthy Choice merger
2. Any superset of a market is a market

  - *Brown Shoe* "practical indicia" tests
    - All are low calorie, single serve, frozen dinners (industry and consumer recognition)
    - IO most significant individual competitors are other LC (high diversion/x-elasticity)
    - Other LC most significant individual competitors are other LC (but not IO) (very high diversion/x-elasticity)

NB: This is not where you want to spend a lot of time. Note the obvious probative facts from the hypothetical and move on.

Relevant product market

- At this point, you are finished with the relevant product market
- If you have time, you could go back and analyze whether all single serve frozen dinners are a relevant market (they are), but it is unlikely to materially advance the analysis

Relevant geographic market

- Relevant geographic market: Nationwide
- Judicial test:
  - Sold nationwide at a uniform price
    - Explicit for IO
    - Assumed for others
  - National advertising
- HMT: Same as above

Here again, this is not where you want to spend a lot of time. Note the obvious probative facts from the hypothetical and move on.

Triggering the *PNB* presumption

- Differentiated products market → Use revenue shares
- 2010 Merger Guidelines

PNB Presumption
Low-Calorie Single-Serve Frozen Dinners

	Sales	Share	HHI contribution
Nestlé (Lean Cuisine)	142.45	54.8%	3000
ConAgra Foods (Healthy Choice)	57.41	22.1%	487
Intelligent Ones	50.00	19.2%	370
Others/Private label (6)	10.22	3.9%	3
	260.08	100.0%	3859

Combined share	41.3%	
Premerger HHI		3859
Delta		849
Postmerger HHI		4708

Triggering the *PNB* presumption

- Judicial precedent
  - Combined share > 30% in *PNB*
  - 2-firm concentration ratio: 76.8% to 96.1%
    (exceeds *PNB*: 43.9% to 59% (change 15.1%))
  - Triggering consistent with subsequent lower court precedent

Precedent	Combined	Delta	Postmerger HHI
FTC v. H.J. Heinz Co., 246 F.3d 708 (D.C. Cir. 2001)	33%	510	5285
United States v. Anthem, Inc., 236 F. Supp.3d 171 (D.D.C.), *aff'd*, 855 F.3d 345 (D.C. Cir. 2017)	47%	537	3000
United States v. H&R Block, Inc., 833 F. Supp. 2d 36 (D.D.C. 2011)	28%	400	4691
United States v. UPM-Kymmene Oyj, No. 03 C 2528, 2003 WL 21781902 (N.D. Ill. July 25, 2003)	20%	190	2990
See In re Evanston Northwestern Healthcare Corp., 144 F.T.C. 1, 379-80 (2007)	35%	384	2739

Additional evidence of anticompetitive effect

- Unilateral effects
  - High diversion of IO to HC suggests an incentive to increase prices for IO
    - Unusual in that
      - Healthy Choice is IO's closest substitute (along with Lean Cuisine)
      - BUT IO is not a substitute for Healthy Choice
      - Can still look at a unilateral price increase for IO given the recapture in Healthy Choice
  - Upward pricing pressure (*Dm*) on IO resulting from merger:
    - Diversion ratio (proportional shares)

$$D_{IO \to HC} = (1 - .5)\frac{22.1}{100 - 19.2} = 13.7\%$$

    - HC gross margin = \$0.56

    - Upward pricing pressure:

$$UPP_{IO} = D_{IO \to HC} m_{HC} = 13.7\% \times \$0.56 = \$0.076$$

Additional evidence of anticompetitive effect

- Unilateral effects
  - Brute force recapture analysis

DATA					BRUTE FORCE CALCULATION	
%SSNIP	5%				%SSNIP for IO	3%
%Actual loss/SSNIP	16.60%		Table 3		$SSNIP (Δp)	$0.0686
%Actual loss/1% SSNIP	3.32%		Calculated		%Actual loss to everything	9.96%
Price	$2.29		Table 2			
Total sales	$50,000,000		Table 1, 4		Retained units	19,659,389
Total units	21,834,061		Calculated		$SSNIP (Δp)	$0.0686
					Gross gain	$1,348,072
%Recapture (all LC)	50.0%		Table 3			
$margin (IO)	$0.69		Table 2		Lost units	-2,174,672
$margin (HC)	$0.56		Table 2		Margin on lost sales	$0.69
					Gross loss	($1,491,204)
					Recaptured units (all LC)	1,087,336
					%Recaptured by HC	27.35%
					Units recaptured by HC	297,403
					Margin on recapture	$0.56
					Gain on recapture	$165,696
					TOTAL GAIN	$22,564

Additional evidence of anticompetitive effect

- Unilateral effects
  - Should note that the merger should produce no upward pricing pressure on Healthy Choice:

$$UPP_{HC} = D_{HC \to IO} m_{IO} = 0 \times \$0.69 = 0$$

Additional evidence of anticompetitive effect

- Coordinated interaction
  - *Question*: Who would be coordinating postmerger?
    - Healthy Choice and Lean Cuisine
  - *Question*: Would the merger enhance the probability or effectiveness of this coordination?
    - *On price*: Given the lack of diversion from Healthy Choice and Lean Cuisine to IO, IO premerger does not create any downward pricing pressure on the other two low calorie frozen dinners
      - Therefore, the merger should not have any effect on price
  - In the writing, may want to go through a more formal analysis if you have the time:
    - Premerger susceptibility
      - Three significant firms with a six-firm fringe
      - A better would be a dominant firm with one significant competitor and 7 fringe firms
        - Given the absence of diversion from HC and Lean Cuisine to IO, IO does not create any downward pricing pressure on the other LCs, making IO a fringe firm
      - Dominant duopoly
      - CONCLUSION: However modelled, the market premerger is susceptible to coordinated effects
    - Postmerger susceptibility

Additional evidence of anticompetitive effect

- Elimination of a maverick
  - A “maverick” is a firm that disrupts coordinated interaction
  - There is no suggestion in the hypothetical of any maverick

Additional evidence of anticompetitive effect

- Exclusionary effects
  - *Question*: Could the merger create an anticompetitive exclusionary effect on grocery store shelf space?
    - The merger increases ConAgra's share in low calorie frozen dinners from 22.1% to 41.3%
    - BUT it only increases ConAgra's share in all frozen dinners from 24.9% to 26.7%
    - ConAgra's bargaining power to gain more frozen food cabinet shelf space most likely comes from its share of all SS frozen dinners, so that acquisition is unlikely to materially increase ConAgra's bargaining power to gain shelf space share and exclude its rivals

Defenses

- Entry
  - Bellisio Foods is poised to enter.
    - Has capability—Productive capacity, distribution, marketing, brand name recognition
    - Cost of entry would not be significant
    - An increase in IO's price would certainly increase BF's incentive to enter
  - Open questions
    - Timing of entry
    - Magnitude of entry
    - Success of entry
  - Problems as a defense
    - Entry defense as such rarely succeeds
    - Combined firm does not control the evidence—Bellisio Foods does
    - Even if BF were to enter immediately, it would still take some time to gear up and produce and promote its product, during which time the combined firm could increase IO's price
  - A better argument is a *limit pricing defense*:
    - The combined firm does not want BF to enter, and therefore will not increase IO's prices or otherwise act anticompetitively after the merger

Defenses

- Efficiencies: Cost savings
  - Fixed cost savings of $6 million per year: Not cognizable
  - Marginal cost reduction for IO: $1.60 to $1.50 or even $1.40
    - This is a cognizable efficiency
    - *Merger specificity*: Comes from a savings in procurement that results from ConAgra's bargaining power given ConAgra's size. Could not be duplicative by IO standing alone.
    - *Verifiability*: Should be able to verify through ConAgra's purchasing records
    - *Sufficiency*: This is an open question

Unilateral effects (from Unit 10 class slides)

- Offsetting marginal cost efficiencies
  - *Query*: What marginal cost reduction would be necessary to offset a one-product unilateral effect?
    - No marginal cost efficiencies:

$$\boxed{\begin{array}{l}\text{Profits from new}\\ \text{sales to new}\\ \text{customers at the}\\ \text{lower price}\end{array}} - \boxed{\begin{array}{l}\text{Reduced profits}\\ \text{from the lower price}\\ \text{to inframarginal}\\ \text{customers}\end{array}} - \boxed{Dm_B} = \boxed{\begin{array}{l}\text{Marginal cost of}\\ \text{increased production}\end{array}}$$

    - Say the marginal cost efficiencies reduce marginal costs by *e* percent. Then:

$$\boxed{\begin{array}{l}\text{Profits from new}\\ \text{sales to new}\\ \text{customers at the}\\ \text{lower price}\end{array}} - \boxed{\begin{array}{l}\text{Reduced profits}\\ \text{from the lower price}\\ \text{to inframarginal}\\ \text{customers}\end{array}} - \boxed{Dm_B} = (1 - e)\boxed{\begin{array}{l}\text{Marginal cost of}\\ \text{increased production}\end{array}}$$

    - To restore the first order condition at original prices and output:

$$Dm_B = ec \quad (= \text{marginal cost reduction})$$

that is, the marginal cost reduction must offset the upward pricing pressure

Defenses

- Efficiencies: Cost savings
  - Upward pricing pressure:

$$D_{IO\rightarrow HC}m_{HC} = 13.7\% \times \$0.56 = \$0.076$$

  - Marginal cost reduction:
    - "From current level of $1.60 to $1.50 or even $1.40)
    - Marginal cost reduction of $0.10 to $0.20
  - Since the marginal cost reduction is greater than the upward pricing pressure, the net effect should be a downward movement in price

The evidence

- Would like the following from IO now and ConAgra later in the process on an "outside counsel only" basis under a joint defense agreement:
  1. Supporting evidence (documents or witnesses who could testify) for all of the predicate facts in the above analysis
  2. A list of the top ten customers of the company for low calories single serve frozen dinner and the company's assessment of how these customers would respond to an FTC inquiry about how they likely would be affected, if at all, by the transaction
  3. A "marketing plan" for the transaction to be rolled out to customers at the time of the announcement of the transaction explaining the reasons for the deal and the benefits customers and ultimate end-users would gain
  4. Any strategic plans or marketing plans prepared over the last three years for single serve frozen dinners generally and low calories single serve frozen dinners in particular
  5. Any marketing or advertising plans prepared over the last three years for single serve frozen dinners generally and low calories single serve frozen dinners in particular

The evidence

6. Any long-range strategic plan prepared over the last three years for single serve frozen dinners generally and low calories single serve frozen dinners in particular
7. Any other company document that identifies competitors for low calorie single serve frozen dinners
8. Any internally or externally prepared market research report prepared over the last three years for single serve frozen dinners generally and low calories single serve frozen dinners in particular
9. Any third-party reports or trade magazine articles that analyze the likely future of the IO
10. Any third-party reports or trade magazine articles that analyze the potential entry of Bellisio Foods into low calorie single serve frozen dinners
11. Any internal analyses or studies regarding the transaction, especially:
    - any possible “4(c)” documents
    - any possible “4(d)” documents
    - any documents that address the rationale for the transaction
    - any documents that address likely present or future changes in any product line as a result of the transaction