DEPARTMENT OF JUSTICE

Merger Guidelines Workshops

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This morning, FTC Chairman Leibowitz announced that, in the coming months, the Federal Trade Commission and the Antitrust Division (collectively, the "Agencies") will be holding public workshops concerning the Horizontal Merger Guidelines. Details about this plan will soon be available on the Federal Trade Commission's web site. In these remarks, I would like to discuss why the Agencies are undertaking this important project.

The Horizontal Merger Guidelines set forth the enforcement policy of the Agencies concerning horizontal mergers and acquisitions. They provide a framework for interpreting and applying the antitrust laws, particularly section 7 of the Clayton Act,[1] section 1 of the Sherman Act,[2] and section 5 of the Federal Trade Commission Act.[3] Section 7 of the Clayton Act provides the most specific standard, providing that mergers are illegal where, "in any line of commerce or in any activity affecting commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly."[4] The Guidelines provide an analytic framework the Agencies use to assess whether a transaction will lead to a substantial lessening of competition and is thus prohibited under U.S. antitrust law.

Let me start by pointing out that the vast majority of mergers are either procompetitive and enhance consumer welfare or are competitively benign. For instance, a recent ten-year review of pre-merger notification filings at the Antitrust Division concluded that (1) only about four percent of the filings resulted in the initiation of a Division investigation, and (2) less than

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1 15 U.S.C. § 18.

2 15 U.S.C. § 1.

3 15 U.S.C. § 45.

4 15 U.S.C. § 18.

half of one percent of the filings resulted in a filed case.[5] Mergers can offer significant consumer benefit through efficiencies and cost reductions that are passed on to consumers in a variety of forms. The focus of the Guidelines is to distinguish between the majority of mergers that raise no competitive concern and the much smaller group of mergers threatening substantial harm to competition.

The ability to substantially lessen competition occurs when a merger creates or enhances market power or facilitates its continued exercise. The core purpose of the Guidelines is to provide a set of tools illuminating whether a given merger is likely to create, enhance, or facilitate market power and thereby have harmful effects on consumers. Those harmful effects can take many forms, including higher prices, slower innovation, lower quality, and reduced product variety. In some cases, a transaction's effects may take the form of reduced incentives to innovate, to cut prices, or to expand consumer choice through product variety. In other cases, the impact on market structure will increase the opportunity for coordinated behavior and raise the risks of the associated anticompetitive effects. Regardless of the particular form of the competitive harm, the bottom line is that mergers that create or facilitate the exercise of unilateral or coordinated market power tend to harm competition and are therefore prohibited by the antitrust laws.

The Guidelines serve the important purpose of providing broad transparency to businesses and the antitrust bar as to how the Agencies approach merger review. Particularly in times of economic uncertainty, providing clear guidance to businesses about enforcement intentions is "good government" that benefits us all.

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[5] *See* U.S. Dep't of Justice, Antitrust Division Workload Statistics: FY 1999-2008, at 2, http://www.usdoj.gov/atr/public/workstats.pdf.

At the same time, however, the Guidelines can only provide what invariably must be a flexible approach to analyzing the competitive effects of mergers. No two mergers are exactly alike, every industry has its idiosyncratic features, and, as the Supreme Court put it in a different antitrust context, "easy labels do not always supply ready answers."[6] Businesses and practitioners should thus appreciate that the enterprise of merger analysis is not an exact science. Rather, it is the effort to utilize analytically rigorous tools that underscore and illuminate competitive concerns. These tools should be used, as the Supreme Court explained with respect to antitrust's rule of reason, to provide "an enquiry meet for the case."[7]

To better express to the business community what enquiries were used to analyze mergers under the antitrust laws, the Department of Justice issued its first Merger Guidelines in 1968.[8] The first revision to the Guidelines occurred fourteen years later in 1982,[9] and the Department issued modified Guidelines two years later in 1984.[10] Eight years later in 1992, the Agencies issued joint Horizontal Merger Guidelines.[11] The Agencies subsequently revised the

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6 Broad. Music, Inc. v. CBS, 441 U.S. 1, 8 (1979).

7 Cal. Dental Ass'n v. FTC, 526 U.S. 756, 780-81 (1999).

8 U.S. DEP'T OF JUSTICE, MERGER GUIDELINES (1968), 4 Trade Reg. Rep. (CCH) ¶ 13,101.

9 U.S. DEP'T OF JUSTICE, MERGER GUIDELINES (1982), 4 Trade Reg. Rep. (CCH) ¶ 13,102.

10 U.S. DEP'T OF JUSTICE, MERGER GUIDELINES (1984), 4 Trade Reg. Rep. (CCH) ¶ 13,103.

11 U.S. DEP'T OF JUSTICE, MERGER GUIDELINES (1992), 4 Trade Reg. Rep. (CCH) ¶ 13,104.

section dealing with efficiencies in 1997.[12] The latest iterative step in this process occurred in 2006, when the Agencies issued the joint Commentary on the Horizontal Merger Guidelines.[13]

Surveying this history, the seventeen years since 1992, when the last significant revision of the Guidelines occurred, mark the longest interval between Guidelines updates since the Department first issued Merger Guidelines in 1968. We intend the workshops to explore whether and how the Agencies should update the Guidelines in light of changes during those seventeen years in economic learning, the development of the case law, and agency practice.

As the Guidelines themselves state, they are not meant to be static documents fixing in stone the Agencies' analytical framework. Instead, as the Guidelines note in their opening section, they "may be revised from time to time as necessary to reflect any significant changes in enforcement policy or to clarify aspects of existing policy."[14] The tools embodied in the Guidelines have evolved in the past and will continue to evolve in the future with the benefit of ongoing economic learning and practical experience.

We intend the workshops to explore whether the Guidelines accurately and clearly describe current agency practice, promoting our goal of greater transparency in the merger-review process. In this regard, I note that many courts indicate that they consider the Guidelines in assessing mergers under the antitrust laws, some finding them more useful than others. The

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12 U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, HORIZONTAL MERGER GUIDELINES § 4 (rev. ed. 1997), *available at* http://www.usdoj.gov/atr/public/guidelines/hmg.pdf [hereinafter 1997 GUIDELINES].

13 U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, COMMENTARY ON THE HORIZONTAL MERGER GUIDELINES (2006), *available at* http://www.usdoj.gov/atr/public/guidelines/215247.pdf [hereinafter 2006 COMMENTARY].

14 1997 GUIDELINES, *supra* note 12, § 0 n.4.

Oracle court, for instance, stated that, while the Guidelines' discussion of unilateral effects in differentiated-products markets "may be a helpful start," it was "not sufficient to describe a unilateral effects claim."[15] This observation suggests that some clarification may be useful. Examples of other recent cases where courts expressly cited the Guidelines include *Staples*,[16] *Swedish Match*,[17] *Chicago Bridge & Iron*,[18] and *Whole Foods*.[19]

The Agencies are also seeking to assess whether the Guidelines should be revised to capture advances in research or evolution in best practices that have taken place over the seventeen years since the Guidelines were last updated in a wholesale fashion. By so doing, the Agencies seek to ensure that the Guidelines set forth clearly and comprehensibly the state-of-the-art techniques that should be used by the Agencies to predict the competitive effects of a merger, promoting our goal of greater accuracy and efficiency in the merger review process. By inviting public comments and holding public workshops, we hope to understand better how the business community perceives the current operation of the Guidelines, to identify any gaps between the Guidelines and actual practice, and simultaneously to seek input on whether and how improvements to the Guidelines can be made.

In the remainder of my remarks, I would like to discuss briefly three broad topics that we anticipate addressing at the workshops: (1) market definition, (2) market concentration, and

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15 United States v. Oracle Corp., 331 F. Supp. 2d 1098, 1117 (N.D. Cal. 2004).

16 FTC v. Staples, Inc., 970 F. Supp. 1066, 1081 (D.D.C. 1997).

17 FTC v. Swedish Match, 131 F. Supp. 2d 151, 167 (D.D.C. 2000).

18 Chi. Bridge & Iron Co. v. FTC, 534 F.3d 410, 431 (5th Cir. 2008).

19 FTC v. Whole Foods Market, Inc., 548 F.3d 1028, 1038 (D.C. Cir. 2008).

(3) competitive effects. The questions for public comment that the Federal Trade Commission will post today provide further details on the topics that will be addressed in the workshops.

The concept of market definition as used in the Guidelines encompasses both product and geographic markets. With regard to product-market definition, consumer demand is the touchstone. As explained in the Agencies' 2006 Commentary on the Horizontal Merger Guidelines, "product market definition depends critically upon demand-side substitution—i.e., consumers' willingness to switch from one product to another in reaction to price changes."[20] That focus on consumers, however, differs from how the term "market" is sometimes used in the business community, where it can refer to a broad range of substitute products and emerging "threats" to a given business. We hope to learn whether clearer language in the Guidelines making this sort of distinction explicit would be useful.

Similarly, the workshops will explore a potential problem with the approach the Guidelines take to geographic market definition. The Guidelines refer to the locations at which goods are produced when discussing how to assess geographic markets.[21] Geographic markets, however, are often based on the locations of customers. For instance, the relevant geographic market may be North America when the concern is over North American customers, even if

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[20] 2006 COMMENTARY, *supra* note 13, at 5; *see also id.* at 6 ("Defining markets under the Guidelines' method does not necessarily result in markets that include the full range of functional substitutes from which customers choose. . . . The Agencies frequently conclude that a relatively narrow range of products or geographic space within a larger group describes the competitive arena within which significant anticompetitive effects are possible."), *id.* at 12 ("The description of an 'antitrust market' sometimes requires several qualifying words and as such does not reflect common business usage of the word 'market.' Antitrust markets are entirely appropriate to the extent that they realistically describe the range of products and geographic areas within which a hypothetical monopolist would raise price significantly and in which a merger's likely competitive effects would be felt.").

[21] 1997 GUIDELINES, *supra* note 12, § 1.21, at 9.

producers from around the world sell the relevant products in North America. The workshops will cover whether and how to clarify in the Guidelines that geographic markets can be defined through reference to customers.

Moving on to market concentration, we plan to seek public comment on the HHI thresholds that define unconcentrated markets where competitive concern is least likely, moderately concentrated markets where competitive concern is only somewhat likely, and highly concentrated markets where competitive concern is greatest. It is no secret that today the HHI thresholds offer relatively little in the way of meaningful guidance to businesses considering merging. We are interested in whether and how the thresholds could be made more useful.

For instance, the Merger Guidelines provide that certain mergers that would result in moderately concentrated industries with HHI thresholds between 1,000 and 1,800 "potentially raise significant competitive concerns."[22] Actual agency practice, however, suggests that only very rarely are mergers resulting in HHI concentration levels below 1,800 challenged.[23] Any gap between actual agency practice and the Guidelines' explanation of that practice is potentially misleading and should be corrected in order to enhance transparency.

Finally, I would like to turn to competitive effects. As I mentioned earlier, a merger's likely competitive effects on consumers and consumer welfare are the core concern of the Guidelines. There are a number of areas concerning competitive effects we anticipate exploring at the workshops. I'll mention three now.

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22 *Id.* § 1.51(b), at 16.

23 FED. TRADE COMM'N & U.S. DEP'T OF JUSTICE, MERGER CHALLENGES DATA, FISCAL YEARS 1999-2003, at 3 tbl.1 (2003), *available at* http://www.usdoj.gov/atr/public/201898.pdf.

First, the Agencies, courts, merging parties, and commentators have all struggled with assessing unilateral effects in markets with differentiated products. This important concept was first introduced into the Guidelines in 1992. Since then, the Agencies and private practitioners have gained extensive experience in analyzing unilateral effects, and a large body of academic and economic learning has grown around the treatment of unilateral effects. This appears to be an area where practice has evolved and where revisions to the Guidelines could be very helpful.

In the 2006 Commentary on the Horizontal Merger Guidelines, the Agencies observed that "[a] merger may produce significant unilateral effects even though a large majority of the substitution away from each merging product goes to non-merging products."[24] The workshops will explore the relationship between that observation and the focus in the Guidelines on "consumers who regard the products of the merging firms as their first and second choices."[25] The workshops will also address more generally how the discussion of unilateral effects and differentiated products in the Guidelines could be improved.

Second, the workshops will consider price discrimination and vulnerable customers. The Guidelines mention price discrimination only briefly[26] and do not address in any detail the situation where competitive effects differ among customer groups. We expect the workshops to address whether and how this aspect of price discrimination should be expanded upon in the Guidelines. This issue is of particular relevance in markets involving both large buyers that may be able to thwart price increases and smaller buyers that might be more vulnerable to increases in

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[24] 2006 COMMENTARY, *supra* note 13, at 27.

[25] 1997 GUIDELINES, *supra* note 12, § 2.21, at 23.

[26] *See id.* §§ 1.12, 1.22.

market power. The D.C. Circuit's reversal of the trial court's "error of law" regarding the implications of price discrimination in the Whole Foods litigation provides a useful recent example from the courts.[27]

Third, we are interested in your views on the use of more direct evidence that is not strictly based on inferences drawn from increases in market concentration. There are several categories of such evidence worth exploring: (1) evidence of the actual, post-merger competitive effects of consummated mergers, (2) evidence of "natural experiments" obtained by looking across different geographic markets, time periods, customer categories, or similar product markets; (3) evidence of the firms' post-merger plans; (4) evidence of customer views of post-merger competition; (5) historical evidence of actual head-to-head competition between the merging firms; and (6) historical evidence of actual or attempted coordination in the industry. Although the Agencies routinely rely heavily on these kinds of evidence to assess competitive effects, the Guidelines address their relevance only in passing and only secondarily, after the relevant market is defined and concentration in that market is measured. Courts also regularly rely on this type of evidence in assessing competitive effects.[28] We are interested in views on whether we should adjust the Guidelines to address explicitly what kinds of direct evidence are pertinent and how they should be weighed.

On this point, I note that in 1986 the Supreme Court relied on evidence of "actual, sustained adverse effects on competition" when analyzing a non-merger restraint of trade in

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27 FTC v. Whole Foods Market, Inc., 548 F.3d 1028, 1037 (D.C. Cir. 2008).

28 *See, e.g.*, FTC v. Swedish Match, 131 F. Supp. 2d 151, 169 (D.D.C. 2000) (relying on evidence of past competition that acted "as a price constraint"); FTC v. Staples, Inc., 970 F. Supp. 1066, 1082 (D.D.C. 1997) (stating that "direct evidence shows that by eliminating Staples' most significant, and in many markets only, rival, this merger would allow Staples to increase prices").

Indiana Federation of Dentists.[29] The Court has not yet had the opportunity to address the potential application of *Indiana Federation of Dentists* in the merger context. Indeed, the Court has not ruled on the merits of a merger since *General Dynamics*,[30] which is now over thirty-five years old. The resulting void in Supreme Court direction helps explain lower court reference to the Guidelines as, in the recent words of the Fifth Circuit Court of Appeals, "persuasive authority when deciding if a particular acquisition violates anti-trust laws."[31] The lack of modern Supreme Court precedent also underscores the need for Horizontal Merger Guidelines that accurately reflect the best economic and legal reasoning.

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I will conclude by observing that, although I am not prejudging the process, if a Guidelines update is deemed worthwhile, I would not at this time anticipate departing from some of the basic elements in the current Guidelines: the use of the hypothetical-monopolist test to define relevant markets, the use of HHI measures of concentration to establish structural presumptions, the centrality of the inquiry into competitive effects, the "timeliness, likelihood, and sufficiency" structure of entry analysis, and the basic treatment of efficiencies and failing firms. Instead, I envision potentially updating the Guidelines to reflect the evolution of practice and advances in learning that have taken place since 1992 largely by (1) clarifying concepts in the current Guidelines that may not be expressed as clearly or fully as they could be, and

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29 FTC v. Ind. Fed'n of Dentists, 476 U.S. 447, 461 (1986).

30 United States v. Gen. Dynamics Corp., 415 U.S. 486 (1974).

31 Chi. Bridge & Iron Co. v. FTC, 534 F.3d 410, 431 n.11 (5th Cir. 2008).

(2) incorporating some of the useful guidance that already exists in the 2006 Commentary on the Horizontal Merger Guidelines into the Guidelines themselves.

Efforts to increase transparency through the Guidelines are part of a broader effort to ensure transparency with respect to the overall workings of the Antitrust Division. As I discussed recently in the context of international competition-law enforcement, transparency is a crucial part of ensuring fairness to parties.[32] Increased transparency can also lead to greater alignment with other competition-law enforcers by providing a clear baseline understanding of our views and intentions and thereby serving as a springboard for further discussion.

This is an exciting project, and I look forward to working with the Federal Trade Commission and all other interested parties in the months ahead.

Thank you.

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[32] Christine A. Varney, Assistant Attorney Gen., U.S. Dep't of Justice, Procedural Fairness (Sept. 12, 2009), *available at* http://www.usdoj.gov/atr/public/speeches/249974.pdf.