

MERGER ANTITRUST LAW

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Georgetown University Law Center
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Tuesdays and Thursdays, 11:10 am – 1:10 pm
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Class 14 (October 17): H&R Block/TaxACT (Unit 9)¹

Once we finish market definition, we will turn to how the DOJ satisfied its burden to make out a prima facie case on the element of likely anticompetitive effect and begin to examine the defendants' rebuttal case.

Review the section of the opinion on whether the DOJ has made out its prima facie case (pp. 124-27). This portion of the opinion applies the *Philadelphia National Bank* presumption. Be sure to reread Section 5 of the 2010 DOJ/FTC Horizontal Merger Guidelines, which gives the agencies' view on how the *PNB* presumption should be implemented. The first two sections of the deck on Anticompetitive Effect in Horizontal Mergers give a quick refresher on the anticompetitive effect element of a Section 7 violation and the *PNB* presumption (slides 3-34).² These early parts of the deck should be easy going since, for the most part, they simply review materials we have already covered. Be sure you have a good sense of how the HHIs work and how the court applied them in *H&R Block* (slide 17) and in merger antitrust cases generally (slides 22-24).³ You might also find interesting how the draft 2023 Merger Guidelines would attempt to change the thresholds for triggering the *PNB* presumption (slides 33-23). There are two changes: (1) the 2023 draft guidelines expand the presumption to “moderately concentrated” markets, where the 2010 guidelines said only that the merger may “potentially raise significant competitive concerns,” and (2) the 2023 draft guidelines create a new trigger where the combined firm has a postmerger share greater than 30% and the change in the HHI is greater than 100.⁴

Also, pay special attention to the last several slides in this section on identifying participants and assigning market shares in relevant markets (slides 35-39) and Sections 5.1 and 5.2 of the 2010 Horizontal Merger Guidelines. Note that the merger guidelines technically can consider nonsellers to be participants in the relevant market and assign them market shares in certain circumstances. In recent years, nonseller market participants have not been a significant factor—or indeed a factor at all—in merger antitrust cases, but you should be aware of the possibility.

¹ A reasonable set of the most important filings in the litigation (including the trial transcript) may be found [here](http://www.appliedantitrust.com) on AppliedAntitrust.com.

² The anticompetitive effects deck repeats a number of slides that you have seen in previous decks. I did this to collect in a single deck all of the relevant slides on anticompetitive effect in horizontal cases.

³ When you are asked (and you will be) whether the HHIs in a hypothetical merger are within the range the courts have accepted as predicating the *PNB* presumption, you will want to compare the hypothetical with the four or five cases with the lowest HHIs that the courts found sufficient to trigger the presumption as well as with the thresholds in the 2010 Merger Guidelines.

⁴ As noted in the class notes, the requirement that the change in the HHI be greater than 100 is largely superfluous. Any merging firms with shares that add to greater than 30% will yield a Δ HHI greater than 100 unless one of the merging firm has a market share of less than 2% (see slide 34).

As a quick aside, it is important to distinguish between nonsellers deemed by the guidelines to be market participants and nonsellers considered to be “potential entrants.” The 1992 guidelines call the former “uncommitted entrants” and the latter “committed entrants” (which the courts call “potential entrants”). As the 1992 guidelines describe uncommitted entrants:

A [nonseller] firm is viewed as a participant if, in response to a “small but significant and nontransitory” price increase, it likely would enter rapidly into production or sale of a market product in the market’s area, without incurring significant sunk costs of entry and exit. Firms likely to make any of these supply responses are considered to be “uncommitted” entrants because their supply response would create new production or sale in the relevant market and because that production or sale could be quickly terminated without significant loss. Uncommitted entrants are capable of making such quick and uncommitted supply responses that they likely influence the market premerger, would influence it postmerger, and accordingly are considered as market participants at both times.⁵

By contrast, the 1992 guidelines define committed entrants as firms that would incur significant sunk costs in entering the relevant market (such as building a specialized factory), have committed to do so, and will likely enter the relevant market as an actual seller within a “timely period” (usually taken to be within two years).⁶ The 1992 guidelines do not consider committed entrants as market participants and instead treat them as part of an entry defense. The 2010 guidelines changed the term “uncommitted entrants” to the more descriptive “rapid entrants.” They also eliminated the 1992 guidelines discussion of identifying rapid entrants and assigning them shares, presumably to give the agencies more flexibility in classifying nonsellers as market participants or alternatively as potential entrants under an entry defense. We will examine the role of nonsellers in more detail in other case studies.

The next section of the opinion analyzes the defendants’ rebuttal arguments. The way the H&R Block/TaxACT opinion is written is somewhat unique (and pedagogically unfortunate): the court concluded its analysis of the DOJ’s prima facie case with nothing more than the *PNB* presumption. It did not follow the rubric of the 2010 DOJ/FTC Horizontal Merger Guidelines and look at the other evidence the DOJ presented to strengthen the *PNB* presumption.⁷ Instead, the court flipped the supporting theory and evidence of anticompetitive harm into the second stage of the *Baker Hughes* burden-shifting paradigm. In doing so, the court placed the burden on the defendants of going forward with evidence showing that the coordinated effects and unilateral theories did *not* apply in the case. As far as the evidentiary proceeding was concerned, the flip of the burden did not matter—defendants would have had to present evidence creating a genuine issue of material fact on each of the theories in any event

⁵ U.S. Dep’t of Justice & Fed. Trade Comm’n, Horizontal Merger Guidelines § 1.0 (rev. 1992) (footnote omitted).

⁶ *Id.* § 3.0; *see id.* § 3.2 (“The Agency generally will consider timely only those committed entry alternatives that can be achieved within two years from initial planning to significant market impact.”) (footnote omitted).

⁷ This “strengthening of the *PNB* presumption” is the common way of describing the role of additional evidence of making out the prima facie case of anticompetitive effect. I think that this is a sloppy way of speaking. The evidence strengthens the finding of a prima facie effect, not the *PNB* presumption per se—the presumption is what it is. However, I am not going to buck convention and undoubtedly will slip into speaking of “strengthening the *PNB* presumption” on occasion.

(which is the test of the burden of production)—but it does make the placement of the analysis of coordinated and unilateral effects in the opinion unusual. Subsequent opinions place the analysis of coordinated and unilateral effects after the *PNB* presumption but still in the section analyzing the DOJ’s prima facie case (i.e., in the first stage of *Baker Hughes*), as the 1992 and 2010 merger guidelines do.

The first rebuttal argument of the defendants is that the likelihood of expansion by existing DDIY companies besides Intuit, HRB, and TaxACT will offset any potential anticompetitive effects from the merger. This is an ease of *entry/expansion/repositioning defense*. In an Economics 101 sense, think of a firm increasing price by restricting its output: if the firm faces a downward-sloping demand curve, the inframarginal customers who value the product the most will bid up the price to clear the market and eliminate the excess demand at the original, lower price. The ease of entry/expansion/ repositioning defense is premised on the ability and incentives of other firms—either new, unrelated entrants into the relevant market (entry), incumbent firms already in the relevant market (expansion), or firms in adjacent markets (repositioning)—expanding output in the relevant market to “fill the hole” in output that the merged firm tried to create. Here, the merging firms argued that the smaller DDIY firms already in the DDIY market (especially TaxHawk and TaxSlayer) would have the ability and incentive to expand and fill the hole, thus eliminating the possibility of a price increase resulting from the merger.

The agencies and the courts treat entry, expansion, and repositioning in the same analytical fashion. The general idea is that the firms in question (either individually or collectively) must have the ability and profit-maximizing incentive to produce additional output to fill the hole. In particular, the Merger Guidelines require—and the courts have followed suit—that the output expansion be:

1. *Timely*, that is, “must be rapid enough to make unprofitable overall” the output reduction in the relevant market that otherwise would have increased prices.
2. *Likely*, that is, sufficiently profitable when compared to alternative courses of action by the third-party firms that the firms have a high probability of actually expanding their output if the merging firms (and any other tacitly coordinating firms) attempted to reduce output in the relevant market, and
3. *Sufficient*, that is, the magnitude of the timely and likely output expansion by these third-party firms will be enough to fill the hole.

First, review the class slides on entry/expansion/repositioning in the Downward-Pricing Pressure Defenses class notes (slides 2-11), then read the entry sections of the 2010 Horizontal Merger Guidelines and the 2023 Draft Merger Guidelines (pp. 272-78), and finally read the court’s analysis of the defendant’s expansion argument and evidence (pp. 127-34). The *H&R Block* court’s rejection of the defense is straightforward. We will also see the ease of entry defense in several future case studies.⁸

I should note that merging parties frequently assert an ease of entry/repositioning/expansion defense in merger antitrust investigations and litigations. We will see it in one form or another in

⁸ The Downward Pricing Pressure Defenses deck contains only the ease of entry defense. As we encountered other defenses in later case studies, I will expand the deck to include them.

a number of case studies. As an empirical matter, the ease of entry defense almost never succeeds. It is easy to see how the defense is defeated. If the merging parties advance the defense, the first question the investigating agency asks the merging parties is who is likely to enter. If the parties cannot identify anyone by name, the agency will reject the defense without more as speculative. If the parties identify one or more firms, the investigating agency will (aggressively) interview them and ask (1) whether they have any interest in entering (or expanding or repositioning in) the relevant market and (2) if so, why haven't they done so already at current prices. Most firms respond that they have not considered entering the market, while firms that have considered entry will explain the various reasons why they have not entered. After establishing a lack of interest or reasons for not entering, the investigating agency will ask if the firm would enter if prices in the market increased by 5 percent. The response is almost invariably no. But if the answer is yes, the investigating agency would drill down with detailed questions about how the decision would be made, the likelihood that the firm would in fact decide to enter, how much it would cost to enter, how long it would take the firm to enter, and at what scale the firm would enter, and what market share the firm would expect to attain. The staff would ask leading questions designed to encourage the firm to give conservative answers. Empirically, the evidence resulting from this line of questioning is sufficient to defeat the defense in an investigation. If the matter proceeds to litigation, the government will offer the same evidence to defeat the defense.⁹

To see how courts analyze ease of entry defenses, read the excerpts from *Energy Solutions*, *Sanford Health*, and *Bertelsmann* (pp. 279-85). Pay attention to how the court summarizes the law to be applied and then how the court applies the law to the facts. We will not discuss these cases in class unless you have questions, but they give you valuable insight into how courts explain and apply the coordinated effects theory of anticompetitive harm.¹⁰

Finally, we will discuss the *coordinated effects theory of anticompetitive harm* in horizontal mergers. The general idea of coordinated effects is that a reduction in the number of firms in the market resulting from the merger increases the likelihood that the remaining firms will be successful in tacitly coordinating their pricing decisions to increase the equilibrium market price. The essential characteristic of the coordinating effects theory is that, in addition to the merged firm, some or all of the *other* firms in the market will also increase their prices in the wake of the merger. The behavior of the other firms in this situation is called *accommodating conduct*.

First, read the coordinated effects section of the opinion (pp. 134-41) and Section 7 of the Horizontal Merger Guidelines. The class notes supply the most detail. The first few slides on coordinated effects provided some essential foundation (slides 40-46). You should pay careful attention to the slides introducing the structure-conduct-performance hypothesis, which you will recall from our original discussion of how *Philadelphia National Bank* formed the basis for the *PNB* presumption. With this background, read the sections on coordinated effects in the 2010 Horizontal Merger Guidelines and the 2023 Draft Merger Guidelines (pp. 218-26).

⁹ Not that the evidence necessary to an ease of entry defense is in the hand of third parties, not the merging parties. In paractive, if the merging partice do not control the evidence, they are likely to be defeated on the poin they are trying to prove.

¹⁰ *Exam hint:* These excerpts may give you some ideas about how to draft the relevant portions of the document you prepare from which you can copy on the graded homework assignment and the final exam. Summarizing the relevant law and applying it to the facts in the hypothetical is precisely what you will be asked to do.

The simple Cournot model provides most of the theoretical support for the structure-conduct-performance hypothesis. Read the slides on the model and its results (slides 47-49), but you can skim or skip the proof of the results (slides 50-51). The key takeaway—which you should know—is that the HHI and the market demand elasticity are sufficient statistics to calculate the extent to which market power (measured by the market Lerner index L) exists in the market with n firms, that is:

$$L \equiv \sum_{i=1}^n L_i s_i = \frac{HHI}{|\varepsilon|},$$

where L_i and s_i are the Lerner index and market share, respectively, of firm i . However, you should pay some attention to the theoretical and empirical criticisms of the profit-concentration hypothesis (a good antitrust lawyer should know what they are) (slides 52-56).

The next group of slides on coordinated effects in the class notes examines the evolution of the coordinated effects theory of anticompetitive from its formal introduction in the 1992 Horizontal Merger Guidelines and the significant revision of the theory in the 2010 Horizontal Merger Guidelines (slides 57-80). Then read the judicial treatments of coordinated effects from court opinions in OSF/Rockford Health, Tronox/Cristal, T-Mobile/Sprint, and Penguin Random House/Simon & Schuster (pp. 227-45 and slides 81-86).

There is almost no chance we will finish coordinated effects on Tuesday. We will pick up what we do not finish in Class 15 on Thursday. We will spend the rest of Class 15 on mavericks and unilateral effects.

Enjoy the reading! Email me if you have any questions.