MERGER ANTITRUST LAW

LAWJ/G-1469-05
Georgetown University Law Center
Fall 2024

Tuesdays and Thursdays, 3:30 pm – 5:30 pm
Dale Collins
wdc30@georgetown.edu
www.appliedantitrust.com

CLASS 4 ASSIGNMENT—INSTRUCTOR'S ANSWER

Instructions

Submit by email before class on Thursday, September 5
Send to wdc30@georgetown.edu
Subject line: Merger Antitrust Law: Assignment for Class 4

Assignment

Time: Early 2014
Calls for a memorandum to the client

Safeway has just been approached by Albertsons with a very attractive purchase offer. Safeway, of course, recognizes that no matter how attractive the purchase price, the Safeway shareholders will receive nothing unless the deal closes.

Alice Smith, the general counsel of Safeway (not really), has asked you (an antitrust attorney at Able and Baker LLP) to send her a short memorandum describing how the antitrust laws might apply to the proposed transaction, the process that the FTC will use in reviewing the merger, and the possible outcomes of the review. Smith wants something short but rigorous that she can share with Safeway's senior business people.

NOTE: The transaction is very confidential, so it is important that you do not identify the parties in the memorandum and use code names instead. The client told us that the code name for the transaction is Project Ceres and that the codenames for Albertsons and Safeway are Bertie and Alexandra, respectively. Be sure to use them and not the real names in the memorandum. As a general rule, you should always use the codenames that the client supplies. In any event, never include the real name of the counterparty in a confidential transaction in a memorandum or email. If the client did not give you one, make one up.

If you would like further background information on the Albertsons/Safeway deal, see the optional case study on Canvas or AppliedAntitrust.com. There is no need for you to look at these materials unless you are so inclined. All you need to know for the memorandum is that Albertsons and Safeway are major supermarket chains and that they overlap in some cities.

ALWAYS include a machine-readable legend on every privileged document you write identifying the document as privileged and the applicable privilege(s)

ABLE & BAKER LLP

INSTRUCTOR'S ANSWER
(with marginal comments)

TO: Alice Smith, Esq.
General Counsel, Safeway Inc.

FROM: Dale Collins

Project Ceres

You have asked me to provide you with a short memorandum describing how the antitrust laws might apply to the proposed transaction, the process that the FTC will use in reviewing the merger, and the possible outcomes of the review.

The antitrust laws

Section 7 of the Clayton Act, which is the provision in the federal antitrust laws that regulates mergers and acquisitions, prohibits transactions "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." 15 U.S.C. § 15.

By its terms, Section 7 has three elements: (1) a relevant product market ("line of commerce"), (2) a relevant geographic market ("section of the country"), and (3) an anticompetitive effect ("may be substantially to lessen competition, or to tend to create a monopoly").

The proposed transaction involves a combination of retail supermarket chains, so the relevant product market will be supermarkets. Since retail purchasers are only willing to travel short distances to shop, the geographic markets will be local. Each local market will need to be assessed separately, and a violation in a single local market can be the basis for an injunction blocking the entire deal.

As viewed by the courts and the enforcement agencies today, a transaction has the requisite anticompetitive effect under Section 7 if it threatens, with a reasonable probability, to result in harm to any identifiable group of customers through an increase in price, a decrease in market output, a decrease in product or service quality in the market overall, or a decrease in the rate of technological innovation or product improvement. In the retail supermarket business, harm to customers most likely will occur, if at all, through price increases enabled by the reduction of the number of competitors resulting from the transaction.[1]

Commented [A1]: Many attorneys like to define terms. I find this silly in memoranda (but not in contracts or court documents) where everyone already knows the terms. But when writing for a partner, use that partner's preferred style.

Commented [A2]: "You have asked me" is a great way to start a memorandum of law responding to a question. Then be precise (and concise) in the questions you are answering. I strongly recommend you use this form in this course and in practice. Also, memoranda of law should b formal in style and *not* conversational. Clients pay a meaningful amount of money for these types of memoranda and they should look professional.

Commented [A3]: There is no reason why you should know this, but historically retail food details have been reviewed by the FTC, which regularly alleges supermarkets to be the relevant product market. If you were an associate in a law firm, you would have researched which agency traditionally reviewed these types of details by looking at past litigated cases and consent decrees

[1] A new focus for the FTC in the Biden administration is labor markets. The FTC is aggressively looking for a Section 7 case to challenge on the grounds that it is likely to substantially lessen competition in the input market for employees. The theory has never been applied to mergers. We should keep this theory in mind as we evaluate the Ceres transaction, but the downstream competitive consequences of the acquisition almost certainly will be the primary focus of any investigation or litigation.

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In assessing a retail supermarket transaction for anticompetitive effect, the investigating agency will rely primarily on two types of evidence.

> *Documents and statements of the merging parties*. If the documents of the parties, including any internal analyses of the transaction or memoranda to the board of directors or the statements of company representatives, suggest that the combined firm postmerger will be able to raise prices to customers in some geographic area, the investigating agency will almost surely regard that area as a relevant geographic market in which the merger will have the requisite anticompetitive effect to violate Section 7. Documents or statements to this effect are almost impossible to impeach, and the agencies consider them conclusive evidence against the transaction.[2]

> *The number of realistic alternative suppliers*. In the absence of "bad" documents or statements, the primary determinant of anticompetitive effect will be whether the customers have "enough" realistic third-party alternatives after the transaction's closing to protect themselves from a price increase. The usual rule of thumb today is that in areas where stores of the two merging parties compete for customers, the customers should have at least four and preferably five realistic alternatives to the combined company to avoid a serious antitrust concern.[3] If the investigating agency determines that customers in an overlap area do not have sufficient alternatives, you should expect that the agency will seek divestitures of all of the stores of one or the other merging party in that area to preserve the premerger level of competition, if not seek to block the deal in its entirety.[4,5]

Commented [A4]: I really mean *today*. This is an anachronism in the memorandum, since the assignment set the date as 2014 when the standards were more lenient. If I was true to the 2014 date, I would have said "three and preferably four."

<u>The merger review process</u>

Given its size, this transaction would be subject to the reporting and waiting period requirement of the Hart-Scott-Rodino (HSR) Act. 15 U.S.C. § 18a. Before closing, the parties will each have to file a prescribed report form with the Antitrust Division of the Department of Justice and the Federal Trade Commission. The HSR Act then bars the closing of the transaction for an initial waiting period of 30 calendar days to permit the investigating agency to conduct a preliminary antitrust merger review. In the case of supermarkets and other consumer retail businesses, the FTC will be the reviewing agency.

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[2] The converse is not true. The investigating agencies consider company documents and statements that the merger will not harm competition as self-serving and unreliable unless they are accompanied by a compelling analysis of why the combined firm will either lack the ability or the profit-maximizing incentive to raise prices.

[3] In other words, a five-to-four or six-to-five transaction.

[4] In close cases in a detailed investigation, the investigating agency may analyze the cross-elasticity of demand between the stores of the merging parties in a given area using point-of-sale scanner data from ACNielsen Scantrack Services or IRI Custom Store Tracking, but usually just the number of competitors in the market postmerger are enough. (**Note to students:** We will cover the use cross-elasticity of demand in merger antitrust analysis in a few weeks. I include this footnote just to be complete.)

[5] **Note to students**: I have to hedge on this. As we will see in the next unit, the Biden DOJ, breaking with several decades of agency practice, is refusing to enter into divestiture consent settlements. Instead, it is forcing the merging parties to choose between voluntarily terminating their transaction or litigating the merits in court. The FTC, which traditionally has reviews supermarket mergers, does accept divestiture consent decrees to "fix" problematic horizontal mergers, although its standards for what amounts to an acceptable settlement are very demanding.

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If the FTC decides to conduct a full investigation, it will issue a so-called "second request" to each of the parties for documents and information. These second requests are voluminous, and compliance typically requires four to eight months. Given the size and significance of the parties in this transaction and the large number of local geographic markets in which they both operate, you should expect that the FTC will not be able to finish its investigation in the 30 days of the initial waiting period and that the FTC will issue a second request to conduct an in-depth investigation. The issuance of a second request extends the waiting period for the time it takes the parties to comply plus an additional 30 calendar days. Moreover, you should expect that the FTC will request, and the parties will find it in their interest to give, a commitment not to close the transaction for an additional 30 to 60 days after the waiting period has expired to enable the FTC to complete its investigation and to allow the parties to present the best possible defense of the transaction.

Outcomes of a merger review investigation

There are five possible outcomes at the end of the investigation:

(1) *No enforcement action.* The FTC concludes that the transaction does not present competitive concerns in any local area and closes the investigation without enforcement action.

(2) *Consent settlement*. The FTC concludes that there are some local areas where the transaction presents competitive concerns, and the parties negotiate a consent decree with the FTC requiring them to divest specified stores (and perhaps distribution centers and other assets) in the problematic areas to one or more third-party buyers acceptable to the FTC to resolve the FTC's antitrust concerns. In the Biden administration, the FTC has accepted very few consent decrees to settle an investigation.[6]

(3) *Litigation*. The FTC concludes that there are some local areas where the transaction presents competitive concerns, the FTC and the parties cannot agree on a mutually acceptable consent decree solution for one or more of these areas, and the FTC challenges the transaction by filing a complaint in federal district court seeking a preliminary injunction to block the transaction's closing pending a full adjudication of the merits as well as an administrative permanent injunction blocking the transaction. The FTC will not accept a consent decree that fails to resolve all its concerns. The parties defend the original transaction in court on the merits.

(4) *"Litigate the fix."* The FTC challenges the transaction in court, but the parties do not defend the original transaction but rather "litigate the fix." This means that the parties enter into a definitive purchase agreement to sell certain stores and other assets to a specific divestiture buyer contingent on the closing of the main transaction. The parties then argue in court that this divestiture will eliminate any competitive concerns about the now-restructured transaction. Courts will evaluate the Section 7 legality of the transaction in light of the fix. The divestiture is usually the same one the parties proposed as a consent decree to the FTC during the second request investigation but the FTC rejected.

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[6] By contrast, the Antitrust Division of the Department of Justice has not accepted any consent decrees to settle an investigation since Jonathan Kanter became AAG on November 16, 2021, although the Division was effectively forced by a court to accept a consent decree to settle an ongoing litigation.

The FTC usually makes three arguments against the "fix: (a) there are relevant markets where no stores are divested where the restructured transaction violates Section 7; (b) there are relevant markets in which an insignificant number of stores or other assets are divested so that the restructured transaction violates Section 7; and (c) even assuming that sufficient stores and assets are divested, the divestiture buyer lacks the ability or incentive to operate the divested stores in a manner that preserves the level of premerger competition.

(5) *Terminate the transaction*. The FTC concludes that there are some local areas where the transaction presents competitive concerns, the FTC and the parties cannot agree on a mutually acceptable consent decree, and the parties voluntarily terminate the transaction rather than proceed to litigation.[7]

If you would like, we can prepare an initial document and information request that will enable us to give you a preliminary analysis as to which areas, if any, the FTC is likely to conclude that the transaction presents a substantive antitrust problem and will require divestitures to settle the investigation.

[7] **Note to students:** I did not include a "fix it first" option. That is because, as we discussed in class, the FTC's view on at least some of geographic overlaps is likely to be unpredictable. Besides, Safeway is the seller, and the sell er has no control over a "fix it first" solution.