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The Agencies Release Consolidated Merger Guidelines: Insights from the Latest Signal for Expanded Merger Enforcement

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On July 19, 2023, the Federal Trade Commission (FTC) and the Antitrust Division of the Department of Justice (DOJ) (collectively, the "Agencies") issued a draft update of the Merger Guidelines (hereinafter, the "Proposed Merger Guidelines"), which President Biden forecasted in 2021 an executive order outlining goals of antitrust reform.[1] As their name suggests, merger guidelines outline the framework used by the Agencies to give effect to the antitrust laws that regulate mergers. Merger guidelines do not have the force of law and courts are not obligated to follow them. Rather, they provide guidance on how the Agencies plan to enforce the law. The principal antitrust law governing the regulation of mergers and acquisitions is section 7 of the Clayton Act; it prohibits transactions that may substantially lessen competition or tend to create a monopoly. Section 7 (and other antitrust laws) are what courts are asked to interpret.

The Proposed Merger Guidelines consolidate and replace prior guidance that outlined the framework for the Agencies' analysis of horizontal and vertical mergers and acquisitions.[2] The Agencies are soliciting comments on the Proposed Merger Guidelines until **September 18, 2023**.

The Proposed Merger Guidelines are consistent with the tenor of merger enforcement under the Biden administration. In this respect, they are not surprising. But they provide a clearer window into the Agencies' thinking about how merger enforcement should proceed. If made final in their present form, the Proposed Merger Guidelines not only expand existing avenues for the Agencies to determine that a merger may be unlawful, they attempt to open new ones as well. These Guidelines portend increased antitrust scrutiny and, although touted for their ability to provide a "clear and administrable framework," introduce new concepts that create uncertainty and opportunity for uneven application.

Key Points: Some of the most significant changes include:

- Horizontal merger analysis: The Proposed Merger Guidelines would replace the Horizontal Merger Guidelines of 2010 and would:
  - Define, for the first time, a market share of 30% as the threshold for determining that a firm is "dominant."
  - Lower the thresholds for both market concentration and a merger's effect on the concentration needed to trigger an Agency presumption of illegality.
  - Lower the proof required to establish antitrust markets by allowing the Agencies to sustain their proposed antitrust market with a showing that a hypothetical monopolist of a candidate group of products might worsen any "terms of sale."
  - Create two new paths for determining that a horizontal merger is unlawful, including (1) the ability to rely exclusively on evidence of substantial competition between the merging parties even if the underlying market is not concentrated and the merged firm would have less than 30% share in that market and (2) by demonstrating, without more, that the merger would eliminate a potential entrant or perceived potential entrant.

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Together, these changes would make it easier for the Agencies to define markets and make it difficult for "5-to-4" mergers—i.e., mergers leaving four or fewer competitors post-transaction—to gain antitrust clearance at the Agencies.

- Vertical merger analysis: The Proposed Merger Guidelines expand the ability of the Agencies to challenge so-called vertical mergers—mergers between firms that operate in different levels of the supply chain. Vertical mergers do not change the number of competitors or the merging parties' market shares anywhere in the supply chain. Three key changes include:
  - Announcing that a market share of 50% anywhere in the supply chain is sufficient for the Agencies to determine that a vertical merger affecting this supply chain is unlawful.
  - Broadening the range of potential mechanisms for vertical transactions to harm rivals, including by acquiring products or services not currently used in the supply chain, and, thus, improve a rival's ability to determine the legality of the proposed transaction.
  - Rejecting reputational harms and contractual commitments that would inhibit engaging in the claimed anticompetitive behavior as valid reasons why the merged firm may lack the incentive or ability to harm competition.
- The Proposed Merger Guidelines also create new bases for concluding that a merger—horizontal, vertical or otherwise—may substantially lessen competition, including if the merger:
  - "Entrenches" or "extends" a dominant position into new markets by, for example, increasing switching costs based on the possibility of bundling products and services (similar to the FTC's allegations in its challenge to Amgen/Horizon).
  - "Contribut[es] to a trend towards consolidation" or being part of a series of acquisitions by an acquiring party.
  - Constitutes unlawful cross ownership or common ownership, even where the acquisitions involve minority interests in the target.
  - Has potential effects on buyers and labor (regardless of the effect, if any, on the products at issue and any benefits to sellers in the same market).
  - Displaces or harms competition on or between multi-sided platforms, especially if a platform operator also provides a service or product in connection with the platform, which may create a conflict of interest.

This new framework is the latest signal by the Agencies that merging parties will face increased antitrust scrutiny in their efforts to merge. While the Agencies' guidance is not considered law, courts have cited to past guidelines frequently in their decision-making. Whether courts will continue to rely on the latest version of merger guidelines in their decision-making remains to be seen, but we suspect that merging parties will increasingly test this question through litigation, particularly in light of the Agencies' recent history in district courts around the country.

The Proposed Merger Guidelines Lay the Groundwork for Increased Scrutiny of Mergers and Acquisitions

The FTC and DOJ announced their 51-page Proposed Merger Guidelines as a replacement for the 2010 Horizontal Merger Guidelines and the 2020 Vertical Merger Guidelines.[3] The FTC approved the draft guidelines unanimously (3-0 vote), and each of the Commissioners issued separate supporting statements. In a change from past merger guidelines, the Agencies try to justify the Proposed Merger Guidelines by citing extensively to case law, largely older Supreme Court and circuit court precedents. By our count, of the 114 citations to court cases included in

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the Proposed Merger Guidelines' 107 footnotes, 93 are to cases from the last century, leaving 21 citations to cases post-2000. Curiously, the Proposed Merger Guidelines do not cite to district court decisions even though this is where most merger litigation is resolved.

Overall, the Proposed Merger Guidelines appear to focus on determining the effects on competition by evaluating the merger's possible effects on **competitors**, which has not been the focus of modern antitrust law. Indeed, the Supreme Court made clear in *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 488, 97 S. Ct. 690, 697, 50 L. Ed. 2d 701 (1977) when it quoted *Brown Shoe Co. v. United States*, 370 U.S., at 320, 82 S.Ct., at 1521 (cases that the Proposed Merger Guidelines cite several times) for the proposition that "[t]he antitrust laws . . . were enacted for 'the protection of competition not competitors.'" The Proposed Merger Guidelines also favor organic growth over acquisition, even if organic growth may be riskier, costlier and more time-consuming, or if the two would produce similar effects.

In our view, here are the most significant changes to the Agencies' analytical framework for mergers and acquisitions:

The Proposed Merger Guidelines Include a New (and Easier) Way to Define Antitrust Markets

Merger analysis typically begins with the determination of a relevant market. Market definition identifies the products and services that compete and the geographic area in which this competition occurs. The fundamental question is whether there is enough substitution outside the proposed market to warrant expanding the proposed market (by adding products/services or broadening the geography, or both). Market definition helps identify competitors and facilitates the computation of market shares, which are often used in short-hand screens to help predict the potential competitive effects of a transaction. As mentioned above, the Proposed Merger Guidelines set a 30% threshold for determining that a merged firm is dominant and set a 50% threshold anywhere in the supply chain for Agencies to presume that a vertical merger is unlawful.

Since 1992, the primary quantitative method used by the Agencies to define markets has been the hypothetical monopolist test, which asks, in substance, whether a single supplier (the hypothetical monopolist) of a candidate group of products could profitably impose a small but significant and non-transitory increase in price (SSNIP) on at least one product in the market.[4] If there is enough switching outside the candidate market by affected stakeholders such that the hypothetical monopolist would not benefit from a price increase (because it would not be profitable after the resulting loss in sales), market power in the candidate market does not exist and, consequently, there is no possibility for a merger to harm competition. Consequently, the analysis often involves estimates of cross-elasticity and the impact of any resulting lost sales on profitability.

The Proposed Merger Guidelines add an addition to the hypothetical monopolist test that appears to sidestep quantitative analysis. Under the revisions, Agencies could also define markets where the hypothetical monopolist would likely **worsen terms of sale** (presumably, terms related to quality, quantity, reliability, etc.) for at least one product in the candidate market. Because worsening terms of sale may be difficult to translate into quantitative measures, estimating the potential for substitution based on concepts of quality and reliability may be difficult and, in any case, likely will not include reliable empirical evidence that bears on the claims. This alternative approach should make defining markets easier for the Agencies, which, in turn, will likely increase the likelihood that the Agencies find mergers unlawful using its concentration-based presumptions.

The Proposed Merger Guidelines explain that **bundled products may constitute separate markets** even if the underlying products are sold separately. They also explain that the Agencies will analyze the market for the sale of a product separately from the market for the purchase of the same product, including assessing the effects on competition for the purchase of labor. The Proposed Merger Guidelines indicate that the Agencies are to take a

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flexible, fact-based approach to determine whether a candidate market that includes one or more bundled products, standalone products or both is a relevant antitrust market.

Impact on Horizontal Merger Analysis

The Proposed Merger Guidelines set low thresholds for determining "dominance" and lower the concentration levels that trigger an Agency presumption of illegality, effectively making it difficult to clear "5-to-4" mergers through the Agencies.

After defining the market, the Agencies typically compute market shares to determine market concentration and compare the size of the merged firm relative to other competitors. Since 1982, the Agencies have measured market concentration using the Herfindahl-Hirschman Index (HHI), which is calculated by summing the squares of individual market shares of each firm in the relevant market. By squaring individual shares, the HHI Index accords greater weight to firms with larger shares; for example, the maximum concentration is 10,000, which is the square of a single firm with 100% share of the market.

In another departure from past guidance, the Proposed Merger Guidelines draw a line at which a firm is presumptively "dominant"—30% market share. At the same time, the Proposed Merger Guidelines lower market concentration thresholds that trigger an Agency presumption of illegality by returning them to levels set forth in the 1997 Horizontal Merger Guidelines. Under the Proposed Merger Guidelines, a merger can trigger an Agency presumption of illegality in two ways: (1) if the market is highly concentrated (i.e., results in an HHI concentration of more than 1,800 points) and the merger would increase concentration by at least 100 points, or (2) if the merged firm will be a dominant firm—i.e., a firm with at least 30% market share—where the merger would increase concentration again by at least 100 points.

By comparison, the existing Horizontal Merger Guidelines set a higher line for determining that a market is highly concentrated (HHI concentration of at least 2,500 points) and do not have the bright line 30% trigger.[5] Under the current approach, the Agencies have cleared many 5-to-4 mergers while challenging mergers that left two or fewer competitors (3-to-2s and 2-to-1s). The battleground between the merging parties and the Agencies has often been over 4-to-3 mergers.

The Proposed Merger Guidelines, however, would make 5-to-4 mergers less likely to gain clearance at the Agencies. Consider the following example: Suppose a market has five firms with market shares of **35%, 30%, 20%, 9.9% and 5.1%,** respectively, where #4 proposes to acquire #5. The merger would create a firm with a post-merger share of 15% but the merged firm would remain #4 and **significantly** smaller than each of the remaining firms in the market. Nevertheless, the Agencies would presume that this merger is illegal because the market is highly concentrated (post-merger HHI concentration of **2,750**) and the merger increases concentration by more than 100 points (about 101 points). Consequently, the Proposed Merger Guidelines, if applied faithfully, would result in a determination that this hypothetical merger is unlawful and may, in similar fashion, cement existing competitive positions and imbalances in the marketplace. Apart from organic growth, smaller players may have a hard time overcoming existing competitive gaps under the new framework. Where markets are unconcentrated, the Proposed Merger Guidelines may create a race to becoming the "first mover" because early acquisitions may fall below lines that trigger presumptions of illegality while subsequent acquisitions may not.

Eliminating head-to-head competition or a potential competitor can be sufficient for a merger to be deemed unlawful by the Agencies.

Under the Proposed Merger Guidelines, the Agencies can find a merger unlawful where there is substantial competition between the merging parties even if the underlying market remains unconcentrated post-merger. In determining whether "substantial competition" exists, the Agencies will examine the strategic decision-making of the merging firms, evaluate competitive rivalry over sales (e.g., win/loss data), assess customer substitution

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between the merging firms and consider other factors. The Agencies can conclude that such competition exists if the parties have shaped one another's behavior or have affected one another's sales, profits, valuation or other drivers of behavior.

In the clearest expression yet, the Agencies explain in the Proposed Merger Guidelines the value they place on preserving potential competition. Under the proposed approach, the Agencies can determine that a merger is unlawful if it would eliminate a potential or perceived entrant in a concentrated market. The Agencies' investigation will evaluate whether one of the parties had a "reasonable probability" of entering the relevant market because, if it reaches this conclusion, the Agencies will "usually presume that resulting concentration and other benefits that would have resulted from its entry would be competitively significant."[6]

Impact on Vertical Merger Analysis

***A market share of 50% anywhere in the supply chain is sufficient for the Agencies to determine that a vertical merger affecting this supply chain is unlawful*.**

Vertical mergers are transactions in which the merging parties operate at different levels of the supply chain. In these situations, the merger does not eliminate any head-to-head competition between the merging parties; in other words, the transaction neither changes concentration nor affects the number of providers in the market. Consequently, the Agencies cannot rely on shortcuts such as the merger's effects on market concentration to establish a presumption of illegality, which has been the case in the Agencies' past four litigated vertical merger challenges.[7]

The Proposed Merger Guidelines change the traditional framework by introducing a bright line structural presumption for vertical mergers. Under the Proposed Merger Guidelines, if the merged firm controls 50% of any market within the supply chain, the Agencies can rely on this basis alone to determine that a vertical merger is unlawful. In other words, if a company achieves 50% share in any market, the Proposed Merger Guidelines would find that its attempted acquisition of any other entity in the supply chain regardless of size in presumptively unlawful.

But this is a one-way bright line. If merging parties have market shares below 50% throughout the supply chain, the Agencies may still determine that the merger is unlawful. In these instances, the Agencies' analysis will focus on the merged firm's ability and incentive to harm competition, principally, by weakening or excluding rivals. The Agencies will investigate whether a vertically-integrated company might degrade or limit access to key inputs, products or services in markets within the supply chain. Consequently, the Agencies will assess the market in which the merged firm competes and related products that rivals may use, now or in the future, as part of the supply chain.

In these circumstances, the Agencies may also consider a range of "plus factors," which could render the merger unlawful, including, among other things, the extent of vertical integration already, the intent of the merger and whether the merger can increase barriers to entry. Mergers may also generate Agency concern where the merged firm would gain control over products or services not currently used in the same supply chain but that could be in the future.

As has always been the case in merger analysis, rivals of the merging parties typically provide perspectives on the merger's effects on competition. Given the range of factors and mechanisms that the Agencies can consider in determining whether a merger may weaken a rival, the proposed framework will likely give rivals an even bigger voice in shaping the Agencies' views of vertical mergers.

***Reputational harms and contractual commitments not to engage in the claimed anticompetitive behavior will not be valid reasons for why the merged firm may lack the incentive or ability to harm competition*.**

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Although the Proposed Merger Guidelines outline a sweep of evidence the Agencies will consider in determining whether a vertical merger may lessen competition, they reject common rebuttals as bases for reaching the opposite conclusion. Under the Proposed Merger Guidelines, the Agencies will "give little weight" to contractual commitments made by the merging parties not to engage in the specific behavior alleged to be anticompetitive by the Agencies and will similarly dismiss reputational harms the merging parties may suffer if they were to break those promises.[8] In issuing this guidance, the Agencies reject precedents from recently litigated vertical merger challenges in federal court and before the FTC's administrative law judge, all of which relied heavily on these kinds of behavioral commitments in ruling against the Agencies.[9] Instead, the Agencies will focus on whether the promises made by the parties align with the merging firm's overall profit and valuation maximization incentives.

New Bases for Concluding that a Merger May Substantially Lessen Competition

The Proposed Merger Guidelines also identify new theories under which the Agencies may deem a merger unlawful.

A merger may now be deemed unlawful by the Agencies if it would entrench or extend a dominant position.

A merger may be unlawful if one of the merging firms already has a dominant position, and the Agencies believe the merger may reinforce or extend this dominant position. The stronger the existing "dominant" position—i.e., shares north of 30% or possessing the power to raise price, suppress output or reduce quality—the lower the showing needed that the merger entrenches or extends a dominant position to support a finding of a presumption of illegality. The Agencies may support these claims with evidence that the merger raises entry barriers generally, including, for example, by increasing switching costs (the FTC's lawsuit to challenge Amgen/Horizon is an example of this theory) or depriving rivals the ability to achieve scale. The concerns about bundling seem to take aim at a common practice in the life sciences industry in which prescription drug manufacturers bundle products to offer greater discounts to PBMs, among other stakeholders.

A merger may now be deemed unlawful by the Agencies if it would "contribute to a trend towards consolidation," is part of a series of acquisitions by an acquiring party, or constitutes unlawful cross ownership or common ownership.

The Proposed Merger Guidelines instruct that a horizontal merger may be unlawful if it "contributes to a trend toward concentration," including not just under Section 7 of the Clayton Act but also Section 1 of the Sherman Act.[10] To determine if such a trend exists, the Agencies look to existing levels of concentration and the "pace" of consolidation. While the Proposed Merger Guidelines clearly define concentration, they are less clear about how much time can pass between acquisitions for the Agencies to conclude no such trend exists. Without further clarity, we fear that the application of these factors could lead to inconsistent results.

The Proposed Merger Guidelines take a similar approach to serial transactions by the same acquiring party. If an individual transaction is part of a larger pattern of acquisitions, the Proposed Merger Guidelines permit the Agencies to consider the cumulative effect of those acquisitions in their analysis. The Agencies may discover such a pattern by, among other things, examining the firm's history of actual or attempted acquisitions, whether consummated or not.

The Proposed Merger Guidelines also take aim at acquisitions by private equity. In yet another departure from past guidance, the Proposed Merger Guidelines state that (a) acquisitions of minority interests in competitors (cross ownership) and (b) acquisitions of minority interests in competing firms (common ownership) can be unlawful. Although these types of acquisitions do not typically give the acquiring party the ability to control the day-to-day operations of the target, the Proposed Merger Guidelines explain that the acquisition of strategic rights may harm competition, including rights to appoint board members, observe board meetings, veto strategic

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activity or access competitively sensitive information. Accordingly, private equity and other investors can expect greater scrutiny over acquisitions of minority interests where they will not be purely passive investors.

A merger may now be deemed unlawful by the Agencies if it substantially lessens competition in the purchase of goods and services, including labor services.

For many years now, the Agencies have explained that regulation of mergers is not limited to sellers of a good but also focuses on whether a merger creates market power for buyers (monopsony power). The Proposed Merger Guidelines reinforce this idea but also extend the concept to the purchase of labor, an idea featured in President Biden's Executive Order of 2021, section 1. To that end, the Agencies will examine whether a merger may reduce competition in labor markets, including by examining whether the merger may lower wages, slow the growth of wages, worsen benefits or working conditions or otherwise degrade the quality of the workplace.

A merger involving aspects of multi-sided platforms may be deemed unlawful by the Agencies if it reduces competition between platforms, on platforms or displaces a platform.

Consistent with the concerns expressed by the Biden administration and the Agencies about "Big Tech," the Proposed Merger Guidelines outline an approach to analyze mergers involving multi-sided platforms. The Proposed Merger Guidelines say that the Agencies should focus on whether a proposed acquisition may harm competition on or between multi-sided platforms or whether the acquisition could inhibit the ability to displace a multi-sided platform. The Proposed Merger Guidelines highlight the importance of determining the magnitude of a conflict of interest if the platform operator also provides a service or product in connection with the platform and make clear that these types of acquisitions may entrench a platform's dominance. As a result, even small accretions affecting platforms may be deemed unlawful by the Agencies. How the Agencies will distinguish acquisitions that improve a platform's usefulness or usability from those that entrench the position of the platform remains to be seen.

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Overall, the Proposed Merger Guidelines are consistent with the tone of merger enforcement under the Biden administration. They are important because they inform the business community about the range of issues that the Agencies will investigate to determine if a merger is objectionable. The Proposed Merger Guidelines accomplish this by broadening the markers for anticompetitive mergers. The breadth of the issues included in the Proposed Merger Guidelines forecasts closer scrutiny on mergers and acquisitions. Companies contemplating mergers can expect investigations covering a wider range of theories and requests to produce even more information to enable the Agencies to examine these issues in the context of the proposed merger. Unfortunately, with the exception of, perhaps, acquisitions resulting in post-merger shares of less than 30% in markets and post-merger concentration levels below 1,000, the Proposed Merger Guidelines do not offer much clarity about what mergers companies can conclude confidently have relatively little risk of extended Agency review. We will continue to examine the activity of the Agencies to provide insights on these and other issues as they develop.

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[1] Executive Order 14036, July 9, 2021.

[2] The FTC withdrew the 2020 Vertical Merger Guidelines on Sept. 15, 2021, although they remain in effect at the DOJ.

[3] The FTC withdrew the 2020 Vertical Merger Guidelines in 2021 although they remain in effect at the Department of Justice. Press Release, Federal Trade Commission Withdraws Vertical Merger Guidelines and Commentary, (September 15, 2021) https://www.ftc.gov/news-events/news/press-releases/2021/09/federal-trade-commission-withdraws-vertical-merger-guidelines-commentary.

[4] The same process can be used for buyer-focused markets.

[5] Importantly, the current Horizontal Merger Guidelines specify that markets with an HHI of 1500 or lower are "unconcentrated" and markets with an HHI between 1500 and 2500 are "moderately concentrated."

[6] U.S. Dep't of Just. & Fed. Trade Comm'n, Merger Guidelines (Draft for Public Comment), 12 (2023) ("Proposed Merger Guidelines"), **https://www.justice.gov/d9/2023-07/2023-draft-merger-guidelines_0.pdf**

[7] See United States v. AT&T Inc., 310 F. Supp. 3d 161 (D.D.C. 2018); United States v. UnitedHealth Group, Inc., 1:22-cv-00481 (D.D.C. Feb. 24, 2022); In re Illumina Inc., Dkt. No. 9401 (F.T.C. Mar. 30, 2021); In re Microsoft Corp., Dkt.No. 9412, (F.T.C. Dec. 8, 2022).

[8] Proposed Merger Guidelines, 16.

[9] See United States v. AT&T Inc., 310 F. Supp. 3d 161 (D.D.C. 2018); United States v. UnitedHealth Group, Inc., 1:22-cv-00481 (D.D.C. Feb. 24, 2022); In re Illumina Inc., Dkt. No. 9401 (F.T.C. Mar. 30, 2021); In re Microsoft Corp., Dkt.No. 9412, (F.T.C. Dec. 8, 2022).

[10] Proposed Merger Guidelines, 21.

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