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## U.S. Antitrust Agencies Issue Revised Merger Guidelines

On August 19, 2010, the Federal Trade Commission and United States Department of Justice issued revised Horizontal Merger Guidelines.<sup>1</sup> The Guidelines, which outline the enforcement agencies' policies and practices for evaluating mergers of actual or potential competitors under the antitrust laws, were last revised in 1997. The newly issued Guidelines are the outcome of a process that began in September 2009, with the agencies' announcement that they would hold a series of public workshops and solicit public comments on whether and how to update the Guidelines. The agencies invited lawyers, economists, academics, and others to participate in the workshops, including Joe Simons and Dan Crane of Paul, Weiss.<sup>2</sup> In April of this year, the agencies released their proposed revisions to the Guidelines, and solicited further public comments.<sup>3</sup> They received 32 comments on their proposed revisions, including one by Paul, Weiss partner Joe Simons.<sup>4</sup>

### The New Guidelines

Changes to the Guidelines since they were last revised include: updated market concentration thresholds; new discussions of the evidence that enforcement agencies consider in analyzing mergers and the economic and other types of analysis they apply; a new explanation of the role of innovation in merger enforcement; new guidance with respect to mergers of competing buyers; and a new section addressing partial acquisitions, which may impact private equity firms, among others. According to Assistant Attorney General for Antitrust, Christine Varney, the revised Guidelines "better reflect the agencies' actual practices" with respect to merger review.

For the most part, the new Guidelines do not reflect significant changes to the proposed Guidelines released for comment last April. Like the proposed Guidelines, the new Guidelines stress that "merger analysis does not consist of uniform application of a single methodology," but rather is a "fact-specific process through which the Agencies . . . apply a range of

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<sup>1</sup> U.S. Dep't of Justice & Fed. Trade Comm'n, Horizontal Merger Guidelines (Aug. 19, 2010) ("Guidelines"), available at <http://www.justice.gov/atr/public/guidelines/hmg-2010.pdf>.

<sup>2</sup> Joseph J. Simons & Daniel A. Crane, Comments to the Federal Trade Commission and Department of Justice Antitrust Division, *Unified Merger Analysis: Integrating Anticompetitive Effects and Efficiencies, and Emphasizing First Principles* (Nov. 2009), available at <http://www.ftc.gov/os/comments/horizontalmergerguides/545095-00007.pdf>.

<sup>3</sup> See our client alert, *U.S. Antitrust Agencies Propose Revisions to Merger Guidelines* (Apr. 22, 2010), available at <http://www.paulweiss.com/files/upload/22Apr10Airt.pdf>.

<sup>4</sup> Joseph J. Simons, Comments to the Federal Trade Commission and Department of Justice Antitrust Division, *Margins in Merger Analysis* (June 4, 2010) ("Simons Comment"), available at <http://www.ftc.gov/os/comments/hmgrevisedguides/548050-00019.pdf>.

analytical tools to the reasonably available and reliable evidence.”<sup>5</sup> For the first time, the Guidelines include a discussion of the sources and types of evidence that the agencies consider in the course of a merger analysis. In addition to market shares and quantitative measures of market concentration, the types of evidence the agencies take into account include historical data from already consummated mergers in the relevant market or analogous markets, whether the merging parties have been head-to-head competitors in the past, and whether a merger would eliminate a “maverick” firm – *i.e.*, one that has played a disruptive role in the market to the benefit of consumers. As sources of information, the agencies look to the merging parties, as well as to customers and other industry participants, analysts, and observers.

The Guidelines also include a substantially revised discussion of the analytical tools the agencies apply to evaluate a merger’s competitive effects. As before, the Guidelines frame the analysis of competitive effects with the use of a “hypothetical monopolist” test to identify relevant antitrust markets. Unlike prior versions, however, the Guidelines set forth a detailed discussion of techniques for implementing that test and for determining the likely effects of a merger on pricing. One such technique, Critical Loss analysis, was developed by our partner Joe Simons in conjunction with a former chief economist at the Department of Justice Antitrust Division. Though Critical Loss Analysis is well established as a matter of agency practice and has long been acknowledged by the courts, it was never before discussed in the Guidelines. The new Guidelines also include for the first time a reference to Upward Pricing Pressure (“UPP”), an approach to assessing the unilateral effects of a merger on competition that was developed by the chief economists of the FTC and Antitrust Division.

#### **Areas of Controversy**

The role these and other forms of economic analysis in the new Guidelines has proven to be their most controversial aspect. Although the Federal Trade Commission voted unanimously to approve the Guidelines, Commissioner J. Thomas Rosch issued a separate statement criticizing their substance as well as the process that led to their release.<sup>6</sup> Despite some substantial improvements, Commissioner Rosch argues that the Guidelines “do not describe the way that the Bureau of Competition and enforcement staff at the Commission proceed today” and that they “also do not reflect the way that courts proceed” in evaluating mergers. His primary criticism is that the Guidelines overemphasize “economic formulae and models based on price theory,” while understating the importance of “non-price competitive effects, such as how a transaction affects quality, service, innovation, and product variety.” This bias in the Guidelines, Rosch contends, is the inevitable outcome of a process that was led by “economists trained and steeped in price theory.”

One particular area of concern highlighted by Rosch’s statement is that “many of the economic theories in the revised Guidelines are based wholly or partially on margins.” Though the Guidelines acknowledge that the presence of high margins in a particular market does not in itself raise an antitrust concern, Rosch argues that the Guidelines erroneously suggest that high margins may be a sufficient basis from which to draw a “sinister inference” –

<sup>5</sup> Guidelines at 1.

<sup>6</sup> Statement of Commissioner J. Thomas Rosch on the Release of the 2010 Horizontal Merger Guidelines, dated Aug. 19, 2010, available at <http://www.ftc.gov/os/2010/08/100819hmgrosch.pdf>.

namely, that rival firms are engaging in coordination of prices, or that consumer demand in the market is not sensitive to changes in price.

In his comment to the agencies, Paul, Weiss litigation partner Joe Simons likewise raised concerns about the extent to which the Guidelines suggest that the agencies will use the existence of high margins to create a presumption of lack of demand responsiveness, narrow markets, and/or market power.<sup>7</sup> Using margins in this way could result in challenges to mergers on a scale not seen for several decades. Moreover, focusing on margins as a guide to market definition and an indicator of market power may be especially problematic for high-tech industries and firms with substantial fixed and/or R&D costs, like pharmaceutical companies. These industries have already attracted significant antitrust scrutiny from the agencies, and the new Guidelines may pose further challenges in the area of merger enforcement.

#### Changes In Agency Practice?

Whether the new Guidelines will signal any substantial change in agency practice remains to be seen. This depends in part on the extent to which the new Guidelines – and especially some of their more controversial aspects – are adopted by the courts. Despite aiming to provide “more clarity and transparency” with respect to how the agencies review mergers, the Guidelines include the disclaimer that they “are not intended to describe how the Agencies will conduct the litigation of cases they decide to bring.” The new Guidelines undoubtedly provide valuable insights and direction for businesses contemplating transactions that are subject to agency review. More telling, however, may be the merger cases that the agencies choose to litigate going forward and how those cases are received by the courts.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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<sup>7</sup> See Simons Comment, *supra* note 4. See also David Scheffman & Joseph Simons, *Unilateral Effects with Differentiated Consumer Products: A Response to Werden*, The Antitrust Source (Aug. 2010).

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