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Antitrust Agencies Issue Final Version Of New Horizontal Merger Guidelines

On August 19, 2010, the Department of Justice and Federal Trade Commission (the "agencies") released the final revised Horizontal Merger Guidelines ("Guidelines"). The Guidelines, last significantly revised in 1992, set forth the methods the agencies use to assess which mergers between rivals are anticompetitive and thus potentially subject to antitrust challenge.

The agencies set out to revise the Guidelines because, the agencies indicated, the 1992 Guidelines did not accurately reflect how the agencies actually analyze mergers. Although the revised Guidelines leave the central framework for analyzing mergers intact – the agencies will identify relevant markets, assign market shares, determine increases in concentration, and assess entry and competitive effects – the revisions reflect a number of important changes that bring the Guidelines more into line with the process and analysis parties presenting transactions to the agencies will confront.

The analytical approaches embraced by the revised Guidelines suggest that the agencies can be expected to closely scrutinize mergers between producers of differentiated products (industries where quality and brands play an important role), to remain skeptical of entry arguments, and to carefully consider theories of "non-price" anticompetitive effects, including how transactions may retard innovation. As the federal courts have yet to embrace many of the principles the revised Guidelines advance, merging parties in the future may more often face the choice between abandoning transactions that face agency opposition or completing a burdensome merger-review process in the hopes of ultimately convincing the agencies – and if not the agencies the federal courts – that a transaction is competitively benign.

No single analytic framework. The 1992 Guidelines described the "analytical framework and specific standards normally used by the [agencies] in analyzing mergers." The revised Guidelines, by contrast, outline "the principal analytical techniques and the main types of evidence on which the Agencies usually rely to predict whether a horizontal merger may substantially lessen competition" and specifically state that the "Guidelines should be read with awareness that merger analysis does not consist of the uniform application of a single methodology."

De-emphasis of market definition and market shares in favor of other ways of predicting competitive consequences. Reflecting the lack of a "single methodology" for analyzing mergers, the revised Guidelines' most notable change is to make clear that defining a relevant market is no longer a starting point in the analysis or, indeed, essential for concluding that a merger is anticompetitive. Rather, where available, the agencies will consult other reflect sources of information that help predict competitive effects. As a practical matter, this means that market shares will be less helpful in screening which potential transactions are likely to raise significant antitrust issues before the agencies. Nonetheless, courts likely will continue to require the agencies to define markets and analyze market shares when challenging mergers.

Making it easier to define narrower markets. The 1992 Guidelines did not articulate a preference for narrowly- or broadly-defined markets and instead provided a general test. In contrast, the revised Guidelines state that narrowly-defined markets are more likely to be useful than broadly-defined markets. Importantly, the agencies will also be more willing to infer narrow markets from high margins. This means, as a practical matter, high margins on the products of the merging parties are likely to increase, not reduce, agency concerns about a potential merger.

HHI thresholds increased. Although the revised Guidelines de-emphasize market definition, the agencies increased the nominal levels of concentration (as measured by the Herfindahl-Hirschman Index) that raise antitrust concern. Because the agencies rarely challenged mergers with modest increases in concentration, this change is likely to make little practical difference.

Mergers involving differentiated products may be more susceptible to challenge. Although the 1992 Guidelines' differentiated products analysis focused on closeness of competition and the ability of competing firms to re-position their products postmerger, the new Guidelines favor calculations based on evidence of premerger margins and "diversion ratios." The revised Guidelines also eliminated language suggesting a safe harbor for transactions where the postmerger share of the parties was below 35% and where the companies were not the first and second choices for a significant number of buyers in the relevant market. This section is arguably the most controversial aspect of the new Guidelines because it adopts economic theories and techniques not wholly accepted by the economics profession. The practical impact of these methodologies is to make more mergers involving differentiated products likely subject to agency challenge.

Fact-specific approach to entry analysis. Under the 1992 Guidelines, entry had to be timely (within 2 years), likely (profitable) and sufficient (of minimum viable or minimum efficient scale) to assuage concerns that a merger would otherwise have anticompetitive effects. The new Guidelines abandon specificity on timeliness and focus instead on whether the potential entry would be likely to constrain an immediate postmerger price increase. The new Guidelines indicate that entry on a scale smaller than that of one of the merging parties is not likely to be persuasive as a defense, particularly if these smaller entrants are likely to have some competitive disadvantages. This revision could be helpful for defense counsel in litigation contexts by eliminating bright-line rules about how quickly entry must occur. However, the revision reflects agency skepticism that entry will obviate threatened anticompetitive effects.

Innovation competition, partial ownership, and powerful buyer sections added. The 1992 Guidelines did not contain these sections; but innovation, partial ownership, and powerful buyer issues have been a part of merger enforcement for years. Under the revised Guidelines, "[t]he Agencies may consider whether a merger is likely to diminish innovation competition by encouraging the merged firm to curtail its innovative efforts below the level that would prevail in the absence of the merger." The revised Guidelines also explain the circumstances under which the agencies will treat a partial ownership interest as a full-blown acquisition, and identify commonly understood ways in which partial ownership can create competitive issues, specifically (a) even a small investment can permit the investor to exercise control over the investee, (b) partial ownership may mute or eliminate the incentive by the investor to compete against the investee, and (c) access to information may enable at least one of the parties to coordinate previously independent decision-making. Finally, the new Guidelines describe the role that so-called "powerful buyers" have in preventing postmerger price increases, but point out that "the Agencies do not presume that the presence of powerful buyers alone forestalls adverse competitive effects flowing from the merger."

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Because the revised Guidelines reflect already largely-implemented enforcement policies, their impact on actual agency practice will be limited. The changes made to the Guidelines nonetheless point to areas where more merger challenges by the agencies can be expected – most notably, in differentiated products, high technology, and in transactions involving partial ownership. It remains to be seen, moreover, whether the revised Guidelines will lead judges to change the (sometime different) tests that courts employ in ruling on agency challenges to transactions.

For more information, please feel free to contact any member of Ropes & Gray's Antitrust Practice Group or your existing Ropes & Gray attorney.