Insight

FTC and DOJ Publish New Merger (Mis)guidelines

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Executive Summary

- On July 19, 2023, the Federal Trade Commission and the Antitrust Division of the Department of Justice released their long-awaited draft of the updated merger guidelines.
- The draft guidelines call for weakening the agencies' decades-old adherence to the consumer welfare standard of antitrust enforcement in favor of policies designed to quash merger activity, regardless of their consumer benefits.
- The agencies will be challenged to convince the public and, more important, the courts, that enforcement is better served by archaic and often ignored case law than modern practices based on consumer welfare.

Introduction

On July 19, 2023, the Federal Trade Commission (FTC) and the Antitrust Division of the Department of Justice (DOJ) jointly published a draft update of the merger guidelines (DMG). While these guidelines are not law, they provide the business community, antitrust practitioners, and the courts insight into how the agencies assess merger and acquisition compliance with federal antitrust law.

President Biden's executive order (EO) on Promoting Competition in the American Economy issued in July 2021 "encouraged" the FTC and DOJ to review the existing horizontal and vertical merger guidelines and "consider whether to revise those guidelines." In January 2022, the agencies announced their intention to do so.

The first merger guidelines were issued by the DOJ in 1968 and centered on the idea of

market concentration; these guidelines were revised in 1982, 1984, 1992, 1997, and most recently in 2010. With each iteration, the guidelines became more grounded in economics and reflected the guiding principle of the consumer welfare standard.

The new draft guidelines depart from this progression of economic understanding. Instead, the agencies have drafted the guidelines using selective case law designed to quash merger activity, regardless of their competitive benefits. The agencies will be challenged to convince the public and, more important, the courts that competition enforcement is better served by relying on archaic case law rather than modern practices grounded in economics and consumer welfare.

What Prompted the Revision?

In July 2021, President Biden's EO on Promoting Competition in the American Economy "encouraged" the FTC and DOJ to review the existing horizontal and vertical merger guidelines and "consider whether to revise those guidelines."

The Biden Administration issued this directive in the belief that "excessive market concentration" was threatening "basic economic liberties, democratic accountability, and the welfare of workers, farmers, small businesses, startups, and consumers." Despite evidence refuting the claim that markets have become more concentrated, the administration wanted the agencies to "resist[] consolidation."

By January of 2022, the agencies announced their intention to review and revise the guidelines. Between that announcement and the issuance of the DMG, the FTC and DOJ made clear through various policy statements, enforcement actions, and speeches that all of the political priorities would likely be adopted in the new merger guidelines.

Overview of the Draft Merger Guidelines

The DMG has one overarching goal: Quash all merger activity with little regard to the welfare of consumers. The DMG puts into words the reasoning and tactics employed by the agencies since FTC Chair Lina Khan and Assistant Attorney General for the Antitrust Division of the DOJ Jonathan Kanter took their respective helms.

The DMG consists of four sections, outlined below, and several appendices to describe "evidentiary and analytical" tools the agencies often use:

- "The Overview outlines the guidelines in summary form to help the public and market participants identify potential concerns and understand the [a]gencies' approach.
- Section II discusses the application of these Guidelines in further detail.

- Section III identifies some of the tools the [a]gencies use to define relevant markets; and
- Section IV explains how the [a]gencies approach several common types of rebuttal evidence."

The DMG's Section II menu of potential competitive harms – there are 13 of them – ignores the possibility of procompetitive benefits that could result from a merger. Such conditions, coupled with the recently proposed changes to the Hart-Scott-Rodino (HSR) premerger notification program, could leave businesses less likely to propose mergers and acquisitions at the risk of costly litigation and the greater likelihood that a merger will be challenged. Consequently, countless welfare-enhancing mergers will be reconsidered, and possibly abandoned. But again, this is by design.

Effect on Consumers

Notable throughout the DMG is its adoption of a "past is future approach." The DMG ignores modern practices centered on consumer welfare and the evolution of economic learning reflected in each updated set of merger guidelines, but instead relies on archaic and often ignored case law.

The merger guidelines attempt to stop merger activity irrespective of its effects on consumers. Thus, the agencies could discount evidence that a merger would be welfare-enhancing. Efficiencies created through a merger often allow the merged firm to offer cheaper, higher quality, and more innovative products.

A company offering a better product at a lower cost, and likely to increase its market share, may run afoul of the DMG, and thus be challenged by the agencies. The DMG's Section IV, subsection 3 (D. Procompetitive) discusses procompetitive efficiencies, stating that "any benefits claimed by the merging parties are cognizable only if they do not result from the anticompetitive worsening of terms for the merged firm's trading partners. Similarly, efficiencies are not cognizable if they will accelerate a trend toward concentration (see Guideline 8) or vertical integration (see Guideline 6)." In other words, the agencies hold that the firm must pass these claimed efficiencies onto the consumer, perhaps in the form of lower prices. Yet this would create a likely situation where the merged firm can gain market share via these lower prices, violating Guideline 8. Furthermore, the statement is more concerned with the merged firm's "trading partners" than ensuring a merger does not harm consumer welfare.

Will the Courts Accept the New Guidelines?

Even if the DMG is published as a final version, it is not law and has no binding effect on the courts. The DMG only explains how the agencies identify potentially illegal mergers. The agencies will need to convince the public, and more important, the courts, that these guidelines best reflect the law. The agencies' recent track record, specifically that of the FTC, may work against them, however. The FTC has already used some of these theories in cases against Meta, Microsoft, and Illumina/Grail. All have been unsuccessful. The recent reputational damage done to the agencies may be difficult to overcome.

Part of the reason the 2010 horizontal merger guidelines proved so successful is that they were created by an independent, nonpartisan agency focused on consumer welfare, a standard widely cited in court decisions for decades. Former DOJ Deputy Assistant Attorney General for Economic, Antitrust Division and joint DOJ/FTC Horizontal Merger Guidelines working group member Carl Shapiro and former FTC Bureau of Economics Director Howard Shelanski conducted a study to measure the 2010 horizontal merger guidelines' success. They found that "In the 10 years since the FTC and DO[J] issued the 2010 [Horizontal Merger Guidelines] HMGs…At a broad level, we find no instances in which the courts rejected any of the 2010 innovations. Nor do we find any instance in which any aspect of the 2010 HMGS – notably the reduced emphasis on market definition or the higher [Herfindahl-Hirschman Index] HHI thresholds – created an impediment for the DOJ or the FTC in bringing or proving a case in court.… Beyond that, numerous courts have either discussed or expressly accepted key elements of the 2010 revisions, with the clearest impact being the increased acceptance in courts of challenges based on unilateral effects." They concluded: "All of this suggests that the 2010 HMGs will have further influence on the evolution of case law going forward." In other words, the courts readily accepted the revisions.

The DMG, and other merger-related policy positions of the agencies, directly advanced many of the features outlined in the executive order. This could make it difficult to persuade judges that these guidelines reflect the law rather than the priorities of the Biden Administration.

Details of the Draft Merger Guidelines

Section II of the DMG outlines 13 points the agencies will use to identify a potentially illegal merger. While many sections would do nothing to enhance consumer welfare — which should be the agencies' goal — there are a few sections that are particularly troublesome.

Guideline 1: Mergers Should Not Significantly Increase Concentration in Highly Concentrated Markets

There is little evidence to support the idea that markets have become, or have trended

toward, greater concentration. Yet the DMG reverts thresholds measuring market concentration using the Herfindahl-Hirschman Index back to what they were in 1982 when they first appeared in the merger guidelines. The agencies provided no economic justification for doing this. In a footnote, the agencies assert that "The more permissive thresholds included in the 2010 Horizontal Merger Guidelines reflected that the agency practice, rather than a judgment of the appropriate thresholds for competitive concern or the requirements of the law."

In previous guidelines, structural presumption was only part of a more complete analysis. The 2010 HMG noted that "market shares may not fully reflect the competitive significance of firms in the market or the impact of the merger. They are used in conjunction with other evidence of competitive effects." The DMG states that a post-merger HHI exceeding 1,800 and a change greater than 100 is considered highly concentrated and "triggers a structural presumption that the merger may substantially lessen competition or tend to create a monopoly." Furthermore, a merged firm's market share of more than 30 percent and a change in HHI greater than 100 "presents an impermissible threat of undue concentration regardless of the overall level of market concentration." These values ignore the limitations of concentration measures that were understood in the previous guidelines.

Guideline 4: Mergers Should Not Eliminate a Potential Entrant in a Concentrated Market

Startup firms face many challenges, including sufficient funding, just to gain access to a market. Many firms rely on venture capital. Before a venture capitalist makes an investment in a startup, however, it is common to plot an exit strategy. Survey data showed that 58 percent of startups cited being acquired as a realistic long-term goal for their company compared to 17 percent wanting to go public via an initial public offering. Only 14 percent planned to stay private.

Challenging mergers that would eliminate a potential entrant, even if the market is concentrated, could have a chilling effect on startup activity if this option is no longer available.

Guideline 9: When a Merger is Part of a Series of Multiple Acquisitions, the Agencies May Examine the Whole Series

This section of the DMG is directly related to the recently proposed changes to the HSR filing form. Currently, the form requires the acquiring firm to disclose prior acquisitions made within the last five years based on certain criteria. The agency will expand the scope by requiring the acquired entity to do the same and extend the time frame from five to 10 years.

This specific section likely targets large tech firms that routinely acquire smaller firms and bring the acquired firm's products to market in a more efficient manner.

Using historical acquisitions to evaluate a new merger proposal does little to measure the effects on competition and protect consumers.

Guideline 11: When a Merger Involves Competing Buyers, the Agencies Examine Whether It May Substantially Lessen Competition for Workers or Other Sellers

The effect of mergers on workers is formally recognized in the merger guidelines for the first time. This addition was the result of several points focused on workers found in the Biden EO.

The proposed changes to the HSR also focused on labor, requiring businesses to disclose workplace-related safety violations by both the acquiring firm and the acquired firm. The agencies asserted that such measures "may be indicative of concentrated labor markets where workers do not have the ability to easily find another job."

Conclusion

The FTC and DOJ's long-awaited draft of updated merger guidelines call for weakening the agencies' decades-long adherence to the consumer welfare standard of antitrust enforcement. In its place, the agencies have designed the DMG to quash merger activity, regardless of its consumer benefits.

Abandoning modern practices based on economic understanding and consumer welfare for a "past is present" approached based on archaic case law will make it difficult for the agencies to convince the courts to accept the DMG.