Insight

Despite Success, Merger Remedies Face Increased Skepticism at Antitrust Agencies

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Executive Summary

- Key antitrust leaders at Federal Trade Commission (FTC) and Department of Justice have voiced skepticism about business divestiture offers as remedies in merger cases, signaling that these agencies may be poised to limit or even abandon the practice entirely.
- Such a move would ignore the findings of a retrospective analysis of merger remedies from 2006–2012—conducted by the FTC itself—that found overwhelming success in maintaining or restoring competition in the relevant market.
- Abandoning divestiture offers as remedies in merger cases would likely lead to fewer mergers being consummated, ultimately harming consumers who would otherwise benefit from a merged company better equipped to meet their needs.

Introduction

Key antitrust leaders Federal Trade Commission (FTC) Chair Lina Khan, Department of Justice (DOJ) Assistant Attorney General of the Antitrust Division Jonathan Kanter, and FTC Competition Director Holly Vedova have voiced skepticism about the practice of business divestiture offers as remedies in merger cases, signaling that these agencies may be poised to limit or even abandon the practice entirely.

The FTC and DOJ Antitrust Division are charged with enforcing Section 7 of the Clayton Act, which prohibits mergers when their effect may be to lessen competition. When an antitrust agency responsible for evaluating a merger finds that it is likely to produce anticompetitive effects, it may discuss possible remedies and enter into a negotiated settlement with the firms. These settlements may involve a firm's divestiture of an asset or an entire business unit, or some other remedy that would restore or maintain competition in the relevant market. These "fixes" enable the merger to be consummated.

Current rhetoric suggests abandoning such fixes, however. Such a move would ignore the findings of a retrospective study commissioned by the FTC itself, in which the agency reviewed merger remedies from 2006–2012 and found that they produced a high success rate in maintaining or restoring competition in the relevant market.

The antitrust agencies have a history of entering into negotiated settlements involving divestitures and other remedies. Abandoning this practice at a time when the agencies have withdrawn guidance for vertical mergers without replacement, have challenged mergers without showing consumer harm, and are currently in the process of revising the horizontal merger guidelines will sow further uncertainty among businesses. Absent these mergers, consumers will be unable to reap the benefits of a newly formed company better equipped to serve its customers while operating in a competitive market.

Merger Remedies

During an antitrust agency's merger review process, if staff "determines that anticompetitive effects are likely, it will discuss … what it believes an acceptable remedy must include to maintain or restore competition in the markets affected by the merger."

For horizontal mergers, settlements between merging firms and antitrust agencies often include structural remedies, including divestitures of assets or even an entire business unit by the merging firms. In the case of vertical mergers, behavioral remedies that bar the joining firms from engaging in specific conduct are frequently implemented.

In the 2019 horizontal merger case involving T-Mobile and Sprint, the DOJ settled with the two firms after negotiating a "package of divestitures" to be owned and operated by Dish, a third party. Structural remedies included divesting Sprint's prepaid mobile business and certain spectrum assets. The settlement also involved behavioral remedies designed to help with the transition to ensure Dish's newly acquired assets would be able to reestablish any market competition lost via the merger.

More recently, upstream manufacturer and seller of genetic sequencing instruments and consumables, Illumina, proposed a vertical merger with Grail, a downstream cancer testing developer. At issue was that Grail and its competitors rely on Illumina's genetic sequencing instruments in their cancer test development, so the FTC sued to block the merger, arguing the vertically integrated firm would have an incentive to foreclose on Grail's rivals to prevent them from developing the cancer test.

In a pre-trial brief, Illumina and Grail highlighted a behavioral remedy that was already being offered to Grail's competitors as a reason to let the merger proceed. The remedy, called Open Offer, was a 12-year supply agreement in which Illumina would not increase the price of any of the supplied sequencing instruments or consumables; a commitment to, by 2025, "decrease the cost of sequencing on Illumina's highest throughput sequencing instrument, using the highest throughput consumable, by at least 43%, for all customers, regardless of application or use case;" and guaranteed that all customers shall receive "universal" pricing for any new sequencing product, and customers shall receive access to the same sequencing products at the same pricing as Grail under a "most-favored nations" clause.

The FTC's administrative law judge cited the Open Offer in the ruling in favor of Illumina and Grail, stating that the agreement "constrains Illumina from harming Grail's alleged rivals" and that the "FTC staff's argument to the contrary is unconvincing."

Remedies offered upfront by merging companies or remedies negotiated with the antitrust agencies during the review process are practices that ultimately benefit the consumer. Under these arrangements, which antitrust leadership believes should be neglected when considering the legality or mergers, the newly joined companies are better able to serve their customers without limiting competition within the relevant market.

Antitrust Agencies Questioning Remedies

FTC Chair Lina Khan, Assistant Attorney General of the Antitrust Division of the DOJ Jonathan Kanter, and most recently FTC Competition Director Holly Vedova have raised concerns about business divestiture offers as remedies in merger cases.

Referring to these divestiture settlements negotiated between merging firms and the FTC, Khan said "That is not work that the agency should have to do. That's something that really should be fixed on the front end by parties being on clear notice about what are lawful and unlawful deals." Khan added that while the agency hasn't banned the current approach "We're going to be focusing our resources on litigating, rather than on settling."

Kanter echoed this sentiment, arguing that "merger remedies short of blocking a transaction too often miss the mark. Complex settlements, whether behavioral or structural, suffer from significant deficiencies. Therefore, in my view, when the division concludes that a merger is likely to lessen competition, in most situations we should seek a simple injunction to block the transaction." In other words, Kanter does not believe divestitures maintain the pre-merger level of competition in the relevant market.

FTC Bureau of Competition Director Vedova reiterated the skepticism of Khan and Kanter. Vedova said the agency "ha[s] neither the resources nor the mandate to function as an industrial planner. Therefore, parties should expect us to be skeptical and risk averse when considering offers to settle in our merger investigations."

Vedova and Kanter both emphasized the increasing complexity of merger remedies as a reason for the possible change in practice.

Khan, Kanter, and Vedova are making different arguments with the same goal in mind: limiting antitrust agency involvement in negotiating remedy settlements. Such action will likely lead to greater uncertainty in the business community and prevent consumers from realizing the benefits of a merged firm operating in a competitive environment.

FTC Remedy Review

A 2017 report from the FTC's Bureaus of Competition and Economics found that the overwhelming share of merger remedies between 2006 and 2012 were successful at maintaining or restoring competition in the relevant market. The study included "89 Commission merger orders … affecting over 400 markets."

The staff examined 50 of the FTC's remedy orders using a case study method in which agency staff "interviewed buyers of divested assets and the merged firms. Staff also interviewed other market participants and analyzed seven years of sales data gathered from significant competitors." Fifteen remedy orders were evaluated by "examining responses to questionnaires directed to Commission-approved buyers in the relevant transactions." These 15 orders involved mergers affecting supermarkets, drug stores, funeral homes, dialysis clinics, and other health care facilities. Finally, the staff examined 24 remedy orders "affecting the pharmaceutical industry using both internal and publicly available information and data."

Using this case study method to evaluate 50 remedy orders, FTC staff "considered a merger remedy to be successful only if it cleared a high bar—maintaining or restoring competition in the relevant market."

The report outlined the "standard for judging success":

- "A remedy was rated as a success if competition in the relevant market remained at its pre-merger level or returned to that level within a short time (two to three years) after the Commission issued the order."
- "A remedy was rated as a qualified success if it took more than two to three years to restore competition

to its pre-merger state, but ultimately did so. Qualified successes also included markets in which buyers of assets were relatively quickly competitive, but for whom continuing success was difficult because of market shocks or situations in which the market evolved in a way not anticipated by the order."

- "A remedy that did not maintain or restore competition in the relevant market was rated as a failure. Failures happened either because the buyer of the assets never produced the product, or because the buyer (or possibly an expanded fringe competitor or a new entrant in the case of a non-structural order) never attained the competitive effectiveness of the pre-merger owner of the divested assets."

The FTC found that "all of the divestitures involving ongoing business succeeded." They also concluded that "Divestitures of limited packages of assets in horizontal, non-consummated mergers … achieved a success rate of approximately 70%." Overall, the agency found that "80% of the … orders maintained or restored competition," including orders involving vertical mergers.

Using the questionnaire method, the FTC found that the "vast majority of the assets divested under those 15 orders are still operating in the relevant market." The agency added that "with respect to the 24 orders … the majority of buyers that acquired products on the market at the time of the divestiture continued to sell those products. Additionally, all the divested assets relating to products that were in development and not available on the market at the time of the divestiture were successfully transferred to the approved buyer."

While the FTC "identified certain areas in which improvements can be made," the study "confirmed that the Commission's practices relating to designing, drafting, and implementing its merger remedies are generally effective."

Conclusion

Despite the evidence of the effectiveness of merger remedies in maintaining or restoring competition, antitrust agency leaders including Khan, Kanter, and Vedova continue to voice skepticism of the practice.

Ultimately, the consumer will suffer should the FTC abandon its consideration of divestiture offers. Doing so would sow increased uncertainty among businesses and likely result in fewer mergers, depriving consumers of the benefits of a newly formed company better equipped to meet their needs while operating in a market with the same level of competition.