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2023 Merger Guidelines

- Increased Suspicion Over Business Deals -

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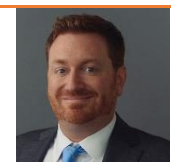

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EXECUTIVE SUMMARY

Shortly before the New Year, the U.S. Department of Justice and the Federal Trade Commission (collectively, the "Agencies") released their long-anticipated 2023 Merger Guidelines that describe the analytical framework the Agencies will use to assess whether mergers and acquisitions are likely to substantially lessen competition in violation of federal antitrust laws.[1] The Guidelines consolidate and replace both the 2010 Horizontal Merger Guidelines and the 2020 Vertical Merger Guidelines. They also reflect an overhaul of antitrust merger enforcement.

The Agencies organize their Guidelines around eleven principles, or "guidelines," that contain rebuttable structural presumptions of illegality for certain mergers in certain markets. Several of these guidelines articulate novel or seldom-used legal theories of competitive harm that have not gained widespread acceptance in the courts. As an example, the Guidelines include an expansive discussion of the potential harm to competition by a proposed merger that *might* eliminate potential entrants or nascent competitive threats, but courts have found such theories to be "impermissibly speculative."[2] The theme of "arrest[ing] anticompetitive tendencies in their incipiency," while difficult to objectively assess, prevails across multiple principles in all sections of the Guidelines, including in the Agencies' renewed approach to horizontal mergers.[3]

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In addressing horizontal mergers, the Guidelines extensively discuss the perceived harm arising from the potential of merged firms to eliminate entrants into new markets.[4] Citing dated case law, the Agencies reason that "expansion into a concentrated market via internal growth rather than via acquisition benefits competition."[5] The FTC recently tested this potential competition theory in an unsuccessful challenge to Meta's acquisition of the virtual reality company Within. EimerStahl Insights recently analyzed that case and this theory.[6]

As to vertical mergers, the Guidelines expand the discussion of possible anticompetitive harms to include the potential to prevent the entry of competitors not only in *relevant* markets under investigation but also in *related* markets. The analysis of related markets includes so-called "route to markets," which the

[1] Merger Guidelines, U.S. Dep't of Justice and the Federal Trade Comm'n (December 2023) ("Guidelines"), *available at* https://www.ftc.gov/system/files/ftc_gov/pdf/P234000-NEW-MERGER-GUIDELINES.pdf.

[2] *See, e.g.*, *FTC v. Meta Platforms, Inc.*, 2023 WL 8629125, at *28 (N.D. Cal. 2023) ("To the extent the FTC implies that . . . [Meta] would have inevitably found and implemented some unspecified means to enter the market, the [c]ourt finds such a theory to be impermissibly speculative.") (discussing cases).

[3] *Id*. at 1.

[4] *See, e.g.*, *id*. at 10–13 (discussing Guideline 4).

[5] *Id*. at 11 (citing *Ford Motor Co. v. United States*, 405 U.S. 562 (1972)).

[6] *See* Nathan P. Eimer, Vanessa G. Jacobsen, and John K. Adams, *What In-House Lawyers Need to Know About the Federal Trade Commission's Current Initiatives, Ranging from Merger Enforcement Practices to Artificial Intelligence*, Eimer Stahl Insights, at 5-6 (May 2023) (discussing *Federal Trade Commission v. Meta Platforms Inc.*, No. 5:22-cv-04325-EJD, 2023 WL 2346238, at *20 (N.D. Cal. Feb. 3, 2023)).

Guidelines define as "any way a firm accesses its trading partners."[7] In other words, the Guidelines articulate harms that may occur when a vertical merger combines suppliers, raising the specter that the merged firm might limit market participants' means to access customers, distribution channels, or trading partners. The risk that the vertically merged firm may limit access in this way is sometimes referred to as "foreclosure."[8] The Agencies' increased suspicion over vertical mergers in the Guidelines departs markedly from previous guidelines that viewed vertical mergers as more procompetitive due to synergies that, for example, remove double marginalization.[9]

There are other key points from the Guidelines beyond the expansion of perceived harms resulting from horizontal and vertical mergers. First, the Guidelines significantly lower the market concentration thresholds at which mergers are *presumed* to harm competition. As explained below, a potential merger resulting in more than a 30% market share could be presumptively anticompetitive. Although this is a rebuttable presumption, the Agencies caution that "[t]he higher the [market] concentration," the more "evidence [is] needed to rebut or disprove" anticompetitive harm.[10]

Second, the Guidelines emphasize that "mergers can violate the law when they entrench or extend a dominant position."[11] This might result from a merger involving a "dominant" firm or a merger creating a "dominant" firm. The term "dominant" is widely used in foreign competition law but has no settled meaning in domestic law, demonstrating the extent to which the Agencies borrowed from European concepts of anticompetitive harm to draft the Guidelines. The Agencies explain that they will evaluate not just the "short-term" effects of a merger involving a dominant firm. They will also evaluate the long-term effects of a merger on "industry dynamics," including on investment and innovation.[12] Here, again, the Agencies focus on "nascent competitive threat[s]" involving the acquisition of "a firm that could grow into a significant rival."[13]

In sum, the 2023 Merger Guidelines demonstrate the degree to which the federal government has more aggressively interpreted and enforced our competition laws. Although the Guidelines are not binding, they carry substantial implications for businesses contemplating mergers or acquisitions, as the Agencies' approach to future merger reviews portend investigations of or challenges to transactions. It is less clear, however, whether courts will follow the Guidelines. In support of their expansive interpretation of the antitrust laws, the Agencies rely upon precedent that is either dated or called into question by more recent

[7] *See* Guidelines at 13–16 (discussing Guideline 5).

[8] *Id*. at 13–14 (citing *Illumina, Inc. v. FTC*, 88 F.4th 1036, 1053 (5th Cir. 2023)).

[9] *See, e.g.*, Vertical Mergers Guidelines, U.S. Dep't of Justice and the Federal Trade Comm'n, 2, 11–12 (June 30, 2020) (explaining that "vertical mergers often benefit consumers through the elimination of double marginalization, which tends to lessen the risks of competitive harm"), *available at* https://www.ftc.gov/system/files/documents/public_statements/1580003/vertical_merger_guidelines_6-30-20.pdf.

[10] Guidelines at 6.

[11] *Id*. at 18 (Guideline 6).

[12] *See id*. at 18–21.

[13] *Id*. at 20-21.

jurisprudence and scholarship. Unlike previous guidelines, moreover, the Guidelines do not reflect bipartisan consensus about modern merger analysis and are therefore subject to change under the next administration.

Businesses considering transactions should continue to consult with antitrust counsel early in the process to identify and mitigate risks. Attorneys at Eimer Stahl LLP are closely monitoring these developments and are ready to discuss these issues as applied to your company or transaction.

THE 2023 MERGER GUIDELINES

The 2023 Merger Guidelines "consolidates, revises, and replaces the various versions of Merger Guidelines previously issued by" the Department of Justice and the Federal Trade Commission.[14] They also finalize the draft guidelines from last summer with few substantive changes.[15] The most notable change from the draft guidelines is the deletion of Draft Guideline 6, which announced a structural presumption of illegality for vertical mergers based on market share.[16] The other significant change is the addition of a section—Section 4— that describes the analytical, economic, and evidentiary tools the Agencies will use in their analysis of whether a merger is likely to lessen competition.[17]

The Guidelines proceed in four sections. Section 1 provides the eleven guidelines. Section 2 describes how the Agencies apply each guideline. Section 3 identifies rebuttal evidence that the Agencies consider, and that merging parties can present, to rebut an inference of illegality. Section 4, as mentioned, sets forth a non-exhaustive discussion of tools that the Agencies will use to evaluate the facts, understand the risk of harm to competition, and define relevant markets for the proposed merger.

I. Sections 1 and 2: Presumptions of Prima Facie Concerns (Guidelines 1–6) and Their Application in Specific Settings (Guidelines 7–11)

A core theory of the Guidelines is that Section 7 of the Clayton Act creates an "expansive definition of antitrust liability" for merger enforcement that is designed to "arrest anticompetitive tendencies in their incipiency."[18] The Guidelines therefore emphasize structural presumptions against certain mergers in Guidelines 1 through 6, which identify mergers that "raise[] prima facie concerns."[19] Guidelines 7 through 11 then explain how to apply these "frameworks in several specific settings."[20]

[14] *Id*. at 4.

[15] *See Draft Merger Guidelines*, U.S. Dep't of Justice and the Federal Trade Comm'n (July 2023) ("Draft Guidelines"), *available at* https://www.justice.gov/d9/2023-07/2023-draft-merger-guidelines_0.pdf.

[16] *Compare id*. at 17–18, *with* Guidelines.

[17] *See* Guidelines § 4.

[18] *Id*. at 1.

[19] *Id*. at 2.

[20] *Id*.

1. **Guideline 1**: Mergers Raise a Presumption of Illegality When They Significantly Increase Concentration in a Highly Concentrated Market.
2. **Guideline 2**: Mergers Can Violate the Law When They Eliminate Substantial Competition Between Firms.
3. **Guideline 3**: Mergers Can Violate the Law When They Increase the Risk of Coordination.
4. **Guideline 4**: Mergers Can Violate the Law When They Eliminate a Potential Entrant in a Concentrated Market.
5. **Guideline 5**: Mergers Can Violate the Law When They Create a Firm That May Limit Access to Products or Services That Its Rivals Use to Compete.
6. **Guideline 6**: Mergers Can Violate the Law When They Entrench or Extend a Dominant Position.
7. **Guideline 7**: When an Industry Undergoes a Trend Toward Consolidation, the Agencies Consider Whether It Increases the Risk a Merger May Substantially Lessen Competition or Tend to Create a Monopoly.
8. **Guideline 8**: When a Merger is Part of a Series of Multiple Acquisitions, the Agencies May Examine the Whole Series.
9. **Guideline 9**: When a Merger Involves a Multi-Sided Platform, the Agencies Examine Competition Between Platforms, on a Platform, or to Displace a Platform.
10. **Guideline 10**: When a Merger Involves Competing Buyers, the Agencies Examine Whether It May Substantially Lessen Competition for Workers, Creators, Suppliers, or Other Providers.
11. **Guideline 11**: When an Acquisition Involves Partial Ownership or Minority Interests, the Agencies Examine Its Impact on Competition.

The Guidelines use low thresholds to trigger the structural presumptions that raise "prima facie concerns" over the proposed merger.

Guideline 1, for example, states that "mergers raise a presumption of illegality when they significantly increase concentration in a highly concentrated market."[21] Under this guideline, the Agencies examine the market share of the proposed merger to determine whether there is a presumption of illegality: "a merger that creates a firm with a share over thirty percent is [] presumed to substantially lessen competition or tend to create a monopoly if it also involves an increase in [the Herfindahl-Hirschman Index (HHI)] of more than 100 points."[22] The HHI, which calculates the sum of the squared market share of each competitor in the market, helps measure concentration in a market. Whereas the 2010 Horizontal Merger Guidelines provided that markets with HHIs in excess of 2,500

[21] *Id*. at 2.
[22] *Id*. at 6.

points (out of 10,000) were "highly concentrated,"[23] the 2023 Guidelines lower that amount to 1,800 points.[24] To put this in perspective, the Agencies now take the position that any market with five industry players is presumed to be highly concentrated and therefore suspect in the event of a merger, irrespective of how those parties' market shares are spread or other competitive conditions.[25]

The explanatory note for Guideline 1 contends that the "Supreme Court has endorsed this view and held that 'a merger which produces a firm controlling an undue percentage share of the relevant market, and results in a significant increase in the concentration of firms in that market, is so inherently likely to lessen competition substantially that it must be enjoined in the absence of rebuttal evidence.'"[26] The selective citation to decades-old precedent without discussion of modern antitrust enforcement decisions, which emphasize analysis of relevant markets over raw numbers, further demonstrates how far the Agencies uprooted prior guidelines. It also stands in tension with the Agencies' objective of revising the Guidelines to comport with "modern" market realities.[27]

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The Guidelines then apply their structural presumptions (Guidelines 1–6) to specific settings (Guidelines 7–11) that, in the Agencies' view, raise novel anticompetitive concerns due to modern industries and technologies.

To illustrate, Guideline 9 applies Guidelines 1 through 6 to "platforms," which encompass Big Tech. "When a merger involves a multi-sided platform," Guideline 9 states, "the Agencies examine competition between platforms, on a platform, or to displace a platform."[28] This guideline claims to "protect competition *between* platforms by preventing the acquisition or exclusion of other platform operators that may substantially lessen competition or tend to create a monopoly."[29] One problematic scenario the Agencies seek to prevent under this guideline involves a "common strategy" that arises when a "dominant platform[]" acquires a "smaller platform[]" that "specialize[s]" and "provid[es] distinctive features" to lessen competition in the relevant market.[30] This guideline exemplifies the prevailing theme identified above of the Agencies' efforts to arrest "anticompetitive tendencies in their incipiency."[31]

This guideline also warns against popular roll-up strategies where a firm (*e.g.*, private equity firm) acquires and merges multiple smaller businesses in the same industry into a larger consolidated company. According to the Agencies,

[23] Horizontal Merger Guidelines, U.S. Dep't of Justice and the Federal Trade Comm'n, § 5.3 (Aug. 19, 2010), *available at* https://www.justice.gov/atr/horizontal-merger-guidelines-08192010.
[24] Guidelines at 5–6.
[25] *See* Draft Guidelines at 6 n.26 (providing illustration of five equal firms in the market that equal HHI of 2,000 ($5 \times 20^2 = 2{,}000$)).
[26] Guidelines at 5 (citing *United States v. Phila. Nat'l Bank*, 374 U.S. 321, 363 (1963)).
[27] *Id*. at 4.
[28] *Id*. at 23.
[29] *Id*. at 24-25.
[30] *Id*. at 25.
[31] *Id*. at 1.

"dominant platforms can lessen competition and entrench their position by systematically acquiring firms competing with one or more sides of a multi-sided platform while they are in their infancy."[32] "The Agencies seek to stop these trends in their incipiency."[33]

II. Section 3: Rebuttal Evidence Against Prima Facie Concerns

Although the 2023 Merger Guidelines create structural presumptions of "prima facie concerns," the Agencies describe "rebuttal evidence" that merging parties could show to demonstrate that there would be "no substantial lessening of competition" by the proposed merger.[34] In so doing, the Agencies draw on precedent that considers "'other pertinent factors' that may 'mandate a conclusion that no substantial lessening of competition is threatened by the acquisition,'" notwithstanding the presumptions outlined above.[35] The Agencies offer several specific forms of "rebuttal evidence" in the Guidelines.[36]

- **Failing Firms**, which "defense applies when the assets to be acquired would imminently cease playing a competitive role in the market even absent the merger";
- **Entry and Repositioning**, which "argument posits that a merger may, by substantially lessening competition, make the market more profitable for the merged firm and any remaining competitors, and that this increased profitability may induce new entry"; and
- **Procompetitive Efficiencies**, which "argument asserts that the merger would not substantially lessen competition in any relevant market in the first place."

III. Section 4: The Agencies' Analytical, Economic, and Evidentiary Tools to Evaluate Mergers and Acquisitions

The Guidelines end with Section 4, which describes in detail the "analytical, economic, and evidentiary tools that [] can be applicable to many parts of the Agencies' evaluation of a merger as they apply the factors and frameworks" outlined above.[37] The Guidelines discuss four tools that the Agencies and merging parties can use when assessing the legality of the proposed merger.[38]

- **Sources of Evidence**, which "describes the most common sources of evidence the Agencies draw on in a merger investigation," including, for example, (1) merging parties, (2) customers, workers, industry participants, and observers, (3) market effects in mergers, (4) econometric analysis and economic modeling, and (5) transaction terms;

[32] *Id*. at 25.
[33] *Id*.
[34] *Id*. at 2, 30.
[35] *Id*. at 30 (citing *United States v. Gen. Dynamics Corp*., 415 U.S. 486, 498 (1974)).
[36] *See id*. at 30–33 (citing sources).
[37] *Id*. at 34.
[38] *See id*. at 34–50 (citing sources).

- **Evaluating Competition Among Firms**, which "discusses evidence and tools the Agencies look to when assessing competition among firms," including, for example, (1) strategic deliberations or decisions, (2) prior merger, entry, and exit events, (3) customer substitution, (4) impact of competitive actions on rivals, and (5) impact of eliminating competition between the firms;
- **Market Definition**, which reinforces that the "Agencies identify the 'area of effective competition' in which competition may be lessened 'with reference to a product market (the "line of commerce") and a geographic market (the "section of the country")'" (citing *Brown Shoe Co. v. United States*, 370 U.S. 294, 324 (1962)); and
- **Calculating Market Shares and Concentration**, which "describes how the Agencies calculate market shares and concentration metrics" through both market participants and market shares.