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Client Alert

Antitrust

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FTC and DOJ Announce New Draft Merger Guidelines

On July 19, 2023, the U.S. antitrust enforcers, the Federal Trade Commission ("FTC") and the Antitrust Division of the Department of Justice ("DOJ") (collectively, the "Agencies"), released draft merger guidelines for public comment ("Draft Guidelines").[1] The Draft Guidelines are intended to replace the existing Horizontal Merger Guidelines, last updated in 2010, and the Vertical Merger Guidelines issued in 2020 and provide guidance for both horizontal and vertical mergers.[2]

The Draft Guidelines will not be officially adopted by the Agencies until at least after the public comment period closes on September 18, 2023. Given the Agencies' extensive work in preparation for the issuance of the Draft Guidelines that included public comments and workshops, we do not anticipate significant changes to the Draft Guidelines when they are released in final form ("Final Guidelines").

Regardless of the timing of final adoption, in public statements on enforcement priorities by officials and through recent enforcement actions, the Agencies already have begun to incorporate elements of the Draft Guidelines into practice, including investigations focused on labor markets and nascent competitors in the tech industry. In conjunction with the recently proposed changes to the Hart-Scott-Rodino merger filing process,[3] the Draft Guidelines indicate that the Agencies will continue to scrutinize mergers and acquisitions aggressively, sweeping in more transactions for inquiry and investigation, which will likely lead to longer clearance timelines. The ultimate adoption of the Final Guidelines marks a significant milestone in memorializing the Biden administration's promise of enhanced antitrust scrutiny and enforcement.

POTENTIAL IMPACT OF THE DRAFT GUIDELINES

Through the merger guidelines, the Agencies "explain how [they] seek to identify potentially illegal mergers" to "the public, business community, practitioners, and courts."[4] Thus, the guidelines not only provide a

roadmap for merging parties as to how the Agencies likely will conduct their analysis into a proposed transaction's competitive effects, the Agencies also intend for courts to utilize and cite to the guidelines in issuing decisions. Indeed, courts regularly include citations and analysis from the 2010 Horizontal Merger Guidelines.

To that end, the Draft Guidelines for the first time include references to a number of "binding legal precedent[s]" and Supreme Court decisions. In likely a direct message to courts, the Draft Guidelines note that they "cite binding propositions of law to explain core principles that the Agencies apply in a manner consistent with modern analytical tools and market realities."[5]

Whether courts will ultimately find the Final Guidelines persuasive is a critical future question. Indeed, although the Draft Guidelines cite extensively to decades-old Supreme Court and appellate court decisions, the guidelines do not address recent losses by the Agencies in court decisions such as *United States v. United HealthGroup*, *United States v. United States Sugar Corp.*, *FTC v. Meta Platforms*, *United States v. Booz Allen Hamilton*, and *FTC v. Microsoft.* Thus, for the time being, the Draft Guidelines are instructive for understanding how the Agencies will analyze, investigate, and potentially litigate against proposed transactions but not whether courts will accept this policy overhaul.

Of course, enhanced antitrust scrutiny may in itself lead to abandoned transactions short of litigation. Longer timeframes and more Second Requests may have a chilling effect on parties both during the clearance process and as parties consider acquisitions that have sprouted newly generated antitrust thorns as a result of the revised guidelines.

STRUCTURE OF THE DRAFT GUIDELINES

The Agencies have built the Draft Guidelines around 13 "core guidelines" that "reflect the most common issues that arise in merger review."[6] Most of these principles are simply general restatements of well-accepted concepts, for example, Guideline 2 states "mergers should not eliminate substantial competition between firms." However, the Draft Guidelines' guidance as to how the Agencies will apply these principles in a number of instances marks a more aggressive enforcement position.

In addition, several of the core guidelines memorialize enforcement initiatives announced by officials in the current administration that have met a controversial reception among practitioners and academics. For example, Guideline 11 states, "When a merger involves competing buyers, the Agencies examine whether it may substantially lessen competition, for workers or other sellers," underscoring the Agencies' focus on labor market dynamics and worker welfare.

HIGHLIGHTS OF SIGNIFICANT CHANGES

Some key changes from the 2010 Horizontal Merger Guidelines include the following:

Lowering of HHI measures to establish structural presumption of harm

Under the 2010 Guidelines and new proposed version, a merger is presumed to have anticompetitive effects if it increases market share concentration measures by a certain amount and above a given threshold. The 2010 Guidelines applied the presumption of harm to mergers that result in a "highly concentrated market," defined as a market with a Herfindahl-Hirschman Index ("HHI") measure of at least 2,500 and increased HHI by at least 200 points.[7]

By contrast, the Draft Guidelines define a "highly concentrated market" as one with an HHI of at least 1,800 (returning to the 1982 Guidelines standard) and apply the presumption if the post-merger HHI reaches this 1,800 threshold and

increases the HHI by 100 points. The Draft Guidelines add another, new trigger establishing the presumption of harm: a merger that increases HHI by 100 points and results in a firm with greater than a 30% market share.

Both of these new market concentration tests will sweep in a much larger number of transactions that will be presumed to be illegal under the Draft Guidelines. For example, suppose a hypothetical market with six firms. If the top four firms each have a 20 percent share, and the bottom two firms each with a 10 percent share attempt to merge, the Draft Guidelines presume this transaction to be illegal (i.e., there could be no merger of the smallest 5th and 6th players). Also, with the introduction of the 30% market share threshold, a merger of two firms, one with a 28% share and the other with a 3% share, would be presumptively anticompetitive.

Curbing a firm's "dominant" position

The Draft Guidelines potentially establish new guardrails on the M&A activity of firms with significant market share. As an initial matter, Guideline 7 notes that a "dominant firm" could be a firm that pre-merger has at least a 30 percent market share. Importantly, courts have not defined the concept of "dominance," and certainly a 30 percent threshold falls far below the general judicial determination of monopoly power.[8]

For such dominant firms, Guideline 7 states that the Agencies will examine whether the merger will strengthen existing dominance. Examples include increasing entry barriers, switching costs and interfering with competitive alternatives. Guideline 7 also cites "depriving rivals of scale economies or network effects" and "eliminating a nascent competitive threat." These last two examples likely directly address Agencies' concerns of increasing market power in the high-tech industry and the need for new models and tools for enforcement.

The Agencies will also examine whether the merger will allow the dominant firm to "extend" its dominant position to a related market. According to the Draft Guidelines, a firm could "leverage its position" through tying, bundling or otherwise linking sales of two products, potentially lessening competition in the second market. Recognizing that such conduct is generally legal and often procompetitive, Guideline 7 states that regulators "will not attempt to assess whether such [linking conduct] would itself violate any law, but instead will assess whether such conduct, if it were to occur, may tend to extend the firm's dominant position." Thus, the Guideline signals a more aggressive enforcement stance in expressly considering how typically legal bundling tactics would increase market power in a secondary market.

Stopping a "trend toward concentration"

Guideline 8 further extends the Agencies' hostility to increases in market concentration noting that "mergers should not further a trend toward concentration," and more closely examining markets in which concentration measures have been increasing.

Guideline 8 describes a two-factor analysis. First, the Agencies will consider whether there are indications of either vertical integration or horizontal consolidation. This can be established, for example, for a steadily increasing HHI from 1,000 rising towards 1,800. Second, the Agencies examine whether the merger would increase concentration or the pace of the trend. This can be established, for example, by a change in HHI greater than 200.

Warning on serial acquisitions

Guideline 9 calls out the potential harm from multiple small, serial acquisitions. Even if no single acquisition on its own would harm competition or tend to create a monopoly, the Agencies may examine the entire pattern of transactions as part of an industry trend, as in Guideline 8, or as a specific strategy by the acquiring firm under Guidelines 1-7.

Thus, where the regulators suspect a market-wide roll-up, they may consider historical evidence of a firm's acquisition practices (whether or not in the relevant market at issue). The Agencies may also consider current documents and testimony reflecting plans and strategies for the individual acquisition and "for the position in the industry more broadly."

This change is likely aimed at private equity firms, as a continuation of the agencies' focus on increasing antitrust scrutiny of this industry.

Protecting workers' welfare

The Draft Guidelines memorialize the Agencies' recent focus on labor market issues and worker welfare in Guideline 11. Guideline 11 ostensibly applies to all input suppliers and increases in buyer power emerging from a merger. In that sense, the Draft Guidelines reinforce the statement in the 2010 Guidelines that the Agencies will evaluate whether a merger will enhance market power on the buying side of a market.

However, Guideline 11 discusses this harm almost exclusively in the context of labor markets and worker welfare. The guideline states that a merger's reduction in labor market competition may result in lower wages and benefits or worsened working conditions and that workers may confront significant switching costs if forced to seek alternative employment.

Significantly, Guideline 11 concludes that because of these characteristics, "labor markets are often relatively narrow," signaling that arguments from parties of how employees may find new employment positions in adjacent fields may not find traction. The guideline also expressly states that countervailing efficiencies resulting from a merger (e.g., from eliminating redundant costs and inputs) cannot save a merger that harms workers.

Guideline 11, coupled with the public pronouncements of Agency officials seeking to protect workers impacted by transactions, opens up a new front in merger analysis and enforcement. Indeed, a typical synergy cited in merger planning documents is labor force consolidation and reductions in force. The guideline provides scant guidance as to how the Agencies will analyze harm to workers, but it is apparent that parties now will have to contend with additional challenges in disproving competitive harm and proving up cognizable efficiencies.

CONCLUSION

The Draft Guidelines set forth significant new merger enforcement priorities and analyses that the Agencies seek to utilize. The Draft Guidelines, coupled with the proposed changes to the HSR process, signal further aggressive antitrust scrutiny of mergers by the Agencies, including of transactions that may have generated little interest or investigation in the past.

Importantly, however, whenever the Draft Guidelines are finalized, they are not law. Although the Final Guidelines will provide a statement of the Agencies' enforcement positions, the guidelines will be subject to review by federal courts that have not always been receptive to novel theories of competitive harm.

Finally, keep in mind that the Draft Guidelines will not necessarily result in more successful challenges to deals and transactions being blocked in federal court. Although it seems clear that the Draft Guidelines will result in deals being more closely examined under aggressive new theories of competitive harm, they only reflect the investigative approach that the Agencies are currently using. The Agencies are already employing the framework set forth in the Draft Guidelines in their current review of transactions, and transactions continue to get cleared by the Agencies.

Also, as noted above, courts have not adopted many of the positions articulated in the Draft Guidelines. As a result, effective advocacy before the agencies and the courts will be even more critical in achieving positive results for merger clearance, including rebutting the aggressive new theories the Agencies will be bringing to bear.

King and Spalding will continue monitoring further developments (sure to come) and will provide additional updates.

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Celebrating more than 130 years of service, King & Spalding is an international law firm that represents a broad array of clients, including half of the Fortune Global 100, with 1,300 lawyers in 23 offices in the United States, Europe, the Middle East and Asia. The firm has handled matters in over 160 countries on six continents and is consistently recognized for the results it obtains, uncompromising commitment to quality, and dedication to understanding the business and culture of its clients.

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[1] https://www.ftc.gov/system/files/ftc_gov/pdf/p859910draftmergerguidelines2023.pdf.
[2] The FTC unilaterally rescinded the Vertical Merger Guidelines in September 2021.
[3] https://www.kslaw.com/news-and-insights/ftc-and-doj-jointly-announced-proposed-changes-to-the-hsr-premerger-notification-form
[4] Draft Merger Guidelines at Overview (p. 1).
[5] Draft Merger Guidelines at Overview (pp. 5-6).
[6] The 13 Guidelines are as follows: 1) Mergers should not significantly increase competition in highly concentrated markets; 2) Mergers should not eliminate substantial competition between firms; 3) Merges should not increase the risk of coordination; 4) Mergers should not eliminate a potential entrant in a concentrated market; 5) Mergers should not substantially lessen competition by creating a firm that controls products or services that its rival may use to compete; 6) Vertical mergers should not create market structures that foreclose competition; 7) Mergers should not entrench or extend a dominant position; 8) Mergers should not further a trend toward concentration; 9) When a merger is part of a series of multiple acquisitions, the Agencies may examine the whole series; 10) When a merger involves a multi-sided platform, the Agencies examine competition between platforms, on a platform, or to displace a platform; 11) When a merger involves competing buyers, the Agencies examine whether it may substantially lessen competition for workers or other sellers; 12) When an acquisition involves partial ownership or minority interests, the Agencies examine its compact on competition; 13) Mergers should not otherwise substantially lessen competition or tend to create a monopoly.
[7] HHI is a common measure of market concentration used by the Agencies to determine market competitiveness. The index measures the size of companies relative to the size of the industry they are in and the amount of competitiveness. The HHI is calculated by squaring the market share of each firm competing in a market and then summing the resulting numbers. It can range from close to 0 to 10,000, with lower values indicating a less concentrated market.
[8] *See e.g., Cliff Food Stores, Inc. v. Kroger, Inc.*, 417 F.2d 203, 207 n.2 (5th Cir. 1969) ("It appears that something more than 50% Of the market is a prerequisite to a finding of monopoly."); *Blue Cross & Blue Shield United of Wisconsin v. Marshfield Clinic*, 65 F.3d 1406, 1411 (7th Cir. 1995) ("Fifty percent is below any accepted benchmark for inferring monopoly power from market share.").