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FTC and DOJ Announce Draft Merger Guidelines for Public Comment

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Go-To Guide:

On July 19, 2023, the FTC and DOJ released for public comment draft updated Merger Guidelines.
The Draft Guidelines are not law but instead inform practitioners and the business community on how the federal antitrust agencies analyze mergers and acquisitions to detect and prevent anticompetitive transactions in the modern market.
They reflect an increased focus on enforcement on digital platforms, incremental "roll-up" strategies, the impact of M&A on wages and benefits, and a perception that previous administrations have been overly permissive leading to excessive concentration across the American economy.

The Federal Trade Commission (FTC) and the Department of Justice's Antitrust Division (DOJ) (together, the "Agencies") on July 19, 2023, released draft updated Merger Guidelines (Draft Guidelines) for public comment. The FTC and DOJ's Merger Guidelines aim to describe how the Agencies review mergers to "better reflect how [they will] determine a merger's effect on competition in the modern economy and evaluate proposed mergers under the law." Merger Guidelines were first released in 1968, and have been updated in 1982, 1984, 1992, 1997, 2010, and 2020. Prior to the July 2023 draft release, the Agencies jointly

published separate Guidelines for horizontal mergers and for vertical mergers, most recently in 2010 and 2020, respectively.[1] However, in September 2021 the FTC withdrew the Vertical Merger Guidelines issued during the Trump administration, and, since then, the Agencies have been working toward updating and revising the Guidelines to release a comprehensive set of Guidelines covering all types of mergers and acquisitions.

Comments on the Draft Guidelines will be accepted for 60 days (deadline: Sept. 18, 2023), and the Agencies will consider comments received when finalizing the guidelines. Primarily, the Draft Guidelines seek to provide updates that better reflect how the Agencies identify and prevent anticompetitive transactions in the modern market.

Background

The Draft Guidelines aim to "build upon, expand, and clarify frameworks set out in previous versions" and present a comprehensive set of principles by which the Agencies scope out transactions to determine if they will have an anticompetitive effect. At the outset, the Draft Guidelines set forth an overview of thirteen guiding principles that the Agencies may use when determining whether a merger is unlawfully anticompetitive under the antitrust laws. These principles are not mutually exclusive, and a given merger may implicate multiple principles.

The document then describes in greater depth the frameworks and tools that may be used when analyzing a

merger with respect to each guiding principle. Indeed, in the FTC press release, FTC Chair Lina Khan stated: “With these draft Merger Guidelines, we are updating our enforcement manual to reflect the realities of how firms do business in the modern economy . . . these guidelines contain critical updates while ensuring fidelity to the mandate Congress has given us and the legal precedent on the books.”[2] Similarly, Attorney General Merrick Garland noted: “These updated Merger Guidelines respond to modern market realities and will enable the Justice Department to transparently and effectively protect the American people from the damage that anticompetitive mergers cause.”[3]

13 Guiding Principles

The Draft Guidelines offer 13 guiding principles to explain how the FTC and DOJ analyze a proposed transaction, and where the Agencies view a proposed transaction as having the potential to substantially lessen competition.

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

When reviewing a merger, the Agencies consider whether it would increase concentration in a market, typically using the Herfindahl-Hirschman Index (HHI). While the HHI, as an analytical tool, is a familiar feature of the Guidelines, the thresholds above which the Agencies will view a transaction as problematic have decreased significantly and returned to pre-2010 levels. The Draft Guidelines state that a market will be considered “highly concentrated” at an HHI of 1,800 or greater (a decrease from 2,500). A merger producing (i) an

increase of more than 100 HHI points (a decrease from 200) and (ii) a post-merger HHI exceeding 1,800 will be presumed to be anticompetitive. Similarly, a proposed transaction will be presumed to be anticompetitive if the merged firms' market share is greater than 30% and the change in HHI is greater than 100. These new thresholds represent a significant tightening of horizontal merger review standards.

Implicit in this tightening is the suggestion that the Agencies since 2010 have been overly permissive of transactions, resulting in highly concentrated markets, perhaps in part due to limited Agency resources permitting them to focus only on the most problematic deals. With additional resources, the Agencies intend to tackle a broader scope of transactions that, in the views of current Agency leadership, should have been challenged in the past.

The Agencies rely on several tools to define a relevant market for purposes of calculating concentration levels, and one familiar tool included in previous versions of the Guidelines is the Hypothetical Monopolist Test (HMT). The HMT asks whether a hypothetical profit maximizing firm that was the only present and future seller of a group of products likely would undertake "at least a small but significant and non-transitory increase in price (SSNIP)" for at least one product in the group. The Draft Guidelines expand on this concept to include "other worsening of terms" (i.e., the SSNIPT), which could include "quality, service, capacity investment, choice of product variety or features, or

innovative effort.” Historically, the Agencies have set the threshold of a price of potential concern at 5%, but the Draft Guidelines note that a lower increase may still be problematic.

Guideline 2: Mergers Should Not Eliminate Substantial Competition Between Firms.

When evaluating a proposed transaction, the Agencies will consider the competition that existed between the firms prior to the merger. The more intensely the parties competed prior to the transaction, the more likely the Agencies are to view the proposed transaction as substantially decreasing competition. In other words, in addition to lowering the HHI thresholds, the Draft Guidelines also aim to spotlight the intensity of competition between the parties in horizontal transactions, regardless of market share. “The more the merging parties have shaped one another’s behavior, or have affected one another’s sales, profits, valuation, or other drivers of behavior, the more significant the competition between them.”[4] The Agencies will examine “evidence relating to strategic deliberations or decisions in the regular course of business” that focus on the other party(s) to the transaction. This is similar to the existing analytical notion of whether the merger parties are one another’s “closest competitors.”

As stated in the Appendices to the Draft Guidelines, the Agencies may examine competition for a targeted subset of customers, including those that the merging firms do not target now but could do so after the proposed merger. The same considerations apply to a merger involving one or

more buyers or employers.[5]

Guideline 3: Mergers Should Not Increase the Risk of Coordination.

If a proposed transaction substantially increases the risk of coordination among the remaining firms in a market, the Agencies may determine that the merger is likely to substantially lessen competition. In making this determination, the Agencies’ primary considerations include whether the market is highly concentrated, prior actual or attempted attempts to coordinate in the market, and whether the proposed transaction involves the elimination of a maverick or disruptive competitor.

Secondarily, the Agencies will also focus on the level of transparency in the market, i.e., “if a firm’s behavior can be promptly and easily observed by its rivals,” the strength and speed with which a firm’s competitive efforts to attract new customers can be counteracted by a response from rivals, and whether key players in a market have aligned incentives.[6]

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

The Agencies may view a transaction that eliminates a potential entrant as substantially lessening competition, especially when it occurs in already concentrated market. The Draft Guidelines specify that “[t]he antitrust laws reflect a preference for internal growth over acquisition.”[7] In this analysis, the Agencies will consider the reasonable probability of alternative entry and the likelihood of

deconcentration.

This Guideline sets out an approach to evaluating both actual potential competition and perceived potential competition. While not prevailing on the merits, the federal court in a recent FTC merger challenge accepted that, when properly proven, either actual potential competition or perceived potential competition by an acquiring firm in the target's product market can form a basis for a claim under Section 7 of the Clayton Act.

Guideline 5: Mergers Should Not Substantially Lessen Competition by Creating a Firm That Controls Products or Services That Its Rivals May Use to Compete.

The Agencies may view a transaction as substantially lessening competition if it gives the merged firm control over products or services its rival use to compete, regardless of whether the transaction involves a traditional vertical supply relationship. The Agencies will consider the merged firm's ability and incentive to weaken or exclude rivals, ability to limit access, and the competitive significance of limiting rivals' access. Prior actions by the merging firms to limit rivals' access as well as internal documents will be considered. The Agencies will also scrutinize transactions that may grant the merged entity access to rivals' competitively sensitive information.[8]

Guideline 6: Vertical Mergers Should Not Create Market Structures That Foreclose Competition.

A merger is considered a vertical merger or non-horizontal merger when the transaction involves two (or more) companies that produce goods or services at distinct levels

in a supply chain for the same final product. When analyzing a vertical merger, the Agencies may consider the structure of the supply chain to determine whether the proposed transaction could substantially lessen competition. Specifically, the Agencies see a greater risk of harm to competition when unintegrated rivals have fewer substitutes for the relevant product.

A “foreclosure share” means the share of the relevant market controlled by the merged firm. The Agencies are likely to view a foreclosure share above 50% as substantially decreasing competition. Below a 50% foreclosure share, the Agencies will consider “plus” factors in their analysis, including the trend toward vertical integration, the nature and purpose of the proposed merger, whether the relevant market is already concentrated, and if the merger would increase barriers to entry.

Guideline 7: Mergers Should Not Entrench or Extend a Dominant Position.

A proposed transaction by an already dominant firm may tend to create a monopoly if the transaction extends or entrenches an already dominant market position. Factors the Agencies will consider include increased barriers to entry, increased switching costs, interference with use of alternatives, deprivation of rivals’ scale economies or network effects, and the elimination of a nascent competitive threat, in the latter case “even if the impending threat is uncertain and may take several years to materialize.” The Agencies will also consider whether a proposed transaction may extend the dominant position of a firm into new or

related markets, thereby lessening competition in those markets.

Guideline 8: Mergers Should Not Further a Trend Toward Concentration.

A proposed transaction may substantially lessen competition or tend to create a monopoly if it furthers a trend toward concentration in the relevant market. The Agencies will consider whether the relevant market has a significant trend towards concentration (either horizontal or vertical). To assess whether or not there is such a trend, the Agencies will use factors including whether an increasing HHI exceeds 1,000 and rises toward 1,800 or would result in the exit of significant market players. The Agencies will also consider whether the proposed transaction would increase the current level of concentration or the pace of concentration, through factors such as a change in HHI greater than 200, or otherwise.

This approach suggests that any combination of rivals, however small, could be problematic because, by definition, a merger of two firms that have some competitive overlap in an product market where another merger recently closed could contribute to a “trend.”

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

The Agencies are paying increasing attention to transactions that involve a firm engaging in multiple small acquisitions in similar business areas, and may view such cumulative transactions as anticompetitive, even where no single proposed acquisition would alone substantially lessen

competition or tend to create a monopoly. The Agencies will "examine a pattern or strategy of growth through acquisition by examining both the firm's history and current or future strategic incentives."

This guiding principle appears to be targeting private equity "roll up" strategies where the investment fund initially acquires an anchor target, and then uses it as a platform to acquire multiple additional firms in an effort to expand the anchor target's product portfolio and geographic reach. Many of these "add-on" acquisitions would otherwise fall below the HSR Act's notification thresholds. The Agencies cite as support for its approach to scrutinize these incremental transactions the Supreme Court's *Brown Shoe decision*[9], legislative history of the Clayton Act from 1950[10], and other somewhat outdated legal precedent.

Notably, the Draft Guidelines make multiple references to restricted supply chains, which may contribute to the Agencies' concern over these types of transactions.

Guideline 10: When a Merger Involves a Multi-Sided Platform, the Agencies Examine Competition Between Platforms, on a Platform, or to Displace a Platform.

The Draft Guidelines include a framework for analyzing transactions involving multi-sided platforms, which framework is the first of its kind in the Draft Guidelines. A platform is defined as providing "different products or services to two or more different groups or 'sides' who may benefit from each other's participation."[11]

This guiding principle specifically relates to digital platforms such as social media networks and other platforms that connect users. The Agencies now specify that when considering a proposed transaction, they consider competition *between* platforms, competition *on* a platform, and competition to *displace* the platform.[12] The framework discusses conflicts of interest, wherein a platform operator is also a platform participant, network effects, and the ability of a platform operator to deny its rivals access to critical inputs, such as data which “helps facilitate matching, sorting, or prediction services.”[13]

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

The Draft Guidelines specify that a “merger between competing buyers may harm sellers just as a merger between competing sellers may harm buyers.”[14] The Agencies have shown an increased interest in labor markets, and this guiding principle includes treating employees as a “seller” of labor and a combined firm as a “buyer” of that labor. The Agencies note that they will consider whether there is a risk that a proposed transaction will substantially lessen competition for labor. Labor markets will be viewed relatively narrowly and on a case-by-case basis.

Importantly, the Draft Guidelines state that “benefits to competition among sellers” may not save a transaction from Agency challenge if that transaction might result in lower wages, decreased benefits or worse working conditions for a

defined labor pool.[15]

Guideline 12: When an Acquisition Involves Partial Ownership or Minority Interests, the Agencies Examine Its Impact on Competition.

Acquisitions of partial control (i.e., non-control or minority acquisitions) may substantially lessen competition, depending on the potential to influence decision-making and the potential for that influence to affect competition. The Agencies will focus on three factors: (1) ability to influence the competitive conduct of the target firm; (2) reduction of the incentive of the acquiring firm to compete; and (3) whether the acquisition gives the acquiring firm access to non-public, competitively sensitive information from the target firm.

Guideline 13: Mergers Should Not Otherwise Substantially Lessen Competition or Tend to Create a Monopoly.

The Draft Guidelines are not an exhaustive list of all possible ways a proposed transaction could be viewed by the Agencies as substantially lessening competition or tending to create a monopoly. For all transactions, the Agencies will consider the law and conduct a fact-specific inquiry.

Key Takeaways

The Agencies intend for the Draft Guidelines to provide merging parties with a clearer understanding of the ways in which the Agencies analyze mergers for potential anticompetitive effects. They also serve an advocacy function to educate and encourage courts to refine their analyses of mergers and acquisitions to account for the modern marketplace. Along with the recently proposed

revisions to the HSR reporting requirements and rules, the Draft Guidelines represent a significant tightening of merger enforcement at the Agencies.

Footnotes

[1] *See* Horizontal Merger Guidelines (2010), Aug. 19, 2010, and Vertical Merger Guidelines (2020), June 30, 2020.

[2] FTC and DOJ Seek Comment on Draft Merger Guidelines, July 19, 2023,

[3] *Id*.

[4] Draft Merger Guidelines at 8.

[5] "In this case, the analysis considers whether buyers target suppliers, for example by paying targeted suppliers or workers less, or by degrading the terms of supply contracts for targeted suppliers." *Id*. at 11.

[6] *Id*. at 10. "For example, a firm with a small market share may have less incentive to coordinate because it has more potential to gain from winning new business than do other firms."

[7] *Id*. at 11.

[8] As stated in the Guidelines, "[R]ivals might refrain from doing business with the merged firm rather than risk that the merged firm would use their competitively sensitive business information to undercut them [and as a result] rely on less preferred trading partners or accept less favorable trading terms because their outside options have worsened or are more limited." See Draft Merger Guidelines at 17.

[9] *Brown Shoe Co. v. United States*, 370 U.S. 294, 346 (1962).

[10] H.R. Rep. No. 1191, 81st Cong., 2d Sess. 12-13 (1950).

[11] Draft Merger Guidelines at 23.

[12] *Id*.

[13] *Id*. at 24.

[14] *Id*. at 25.

[15] "Because the Clayton Act prohibits mergers that may substantially lessen competition or tend to create a monopoly in any line of commerce and in any section of the country, a merger's harm to competition among buyers is not saved by benefits to competition among sellers. That is, a merger can substantially lessen competition in one or more buyer markets, seller markets, or both, and the Clayton Act protects competition in any one of them." *Id*. at 26-27.

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