AXINN,
VELTROP &
HARKRIDER LLP

LEGAL DEVELOPMENTS

March 28, 2006

FTC AND DOJ ISSUE JOINT COMMENTARY ON THE HORIZONTAL MERGER GUIDELINES

In the latest in a series of "ongoing efforts to increase the transparency of their decision-making processes," on March 27, 2006, the Department of Justice and the Federal Trade Commission jointly issued a *Commentary on the Horizontal Merger Guidelines.* While the Commentary neither amends nor marks a substantial departure from recent enforcement policy, it does embrace the current administration's stance on merger review, which not only values the potential benefits that mergers can offer the economy, but also favors a rigorous competitive effects analysis over that which relies significantly upon an analysis of market shares and concentration.

In order to "foster deeper understanding regarding antitrust law enforcement," the Commentary provides not only an overview of the legal and analytical standards that the Agencies employ in reviewing mergers for compliance with the antitrust laws, but also an insight beyond that found in the *1992 Horizontal Merger Guidelines* regarding the types of evidence and other information that the Agencies find probative in conducting merger investigations. Importantly, the document also provides case summaries of many leading mergers that serve to illustrate the various points made in the Commentary. It thus offers helpful guidance for analyzing future transactions based upon analogous enforcement precedent.

According to the Commentary, the "Guidelines' analytic framework has proved both robust and sufficiently flexible to allow the Agencies properly to account for the particular facts presented in each merger investigation." As a result, the Agencies have decided that a "revamping of the Guidelines is neither needed nor widely desired at this time" and instead issued the Commentary. In releasing it, the Chairman of the FTC observed: "The merger review process is highly fact-intensive. By explaining how we have applied the Guidelines to actual investigations, the Commentary should foster greater public understanding about the review process, and in doing so, help businesses assess the potential antitrust risks they face when evaluating whether to proceed with a transaction." In the same vein, the head of the Justice Department's Antitrust Division stated that with the Commentary, "[t]he business community can see how the Agencies have applied the Horizontal Merger Guidelines to a wide range of specific factual circumstances."

The Agencies assess the competitive effects of mergers under the framework set forth in the Guidelines, which employ a five-part analysis consisting of: (1) market definition and concentration; (2) potential adverse competitive effects; (3) entry analysis; (4) efficiencies; and (5) failing and exiting assets. As the Commentary provides, the "ordering of these elements in the Guidelines, however, is not itself analytically significant, because the Agencies do not apply the Guidelines as a linear, step-by-step progression that invariably starts with market definition and ends with efficiencies or failing assets." Indeed, as the Commentary points out, on occasion the government will even dispense with an analysis of

Axinn, Veltrop & Harkrider LLP
1370 Avenue of the Americas
New York, NY 10019
Tel: 212 728 2200
Fax: 212 728 2201

90 State House Square
Hartford, CT 06103
Tel: 860 275 8100
Fax: 860 275 8101

1801 K Street, N.W., Suite 411
Washington, DC 20006
Tel: 202 912 4700
Fax: 202 912 4701

Axinn, Veltrop & Harkrider LLP practices in the areas of antitrust and trade regulation, intellectual property and complex litigation. The firm provides ongoing advice and services to Fortune 500 clients in the antitrust aspects of M&A transactions. The firm also counsels clients in a wide range of other areas, including deceptive acts and practices, health care, consumer protection, FDA law and various regulatory areas.

market definition and concentration where there is evidence directly pointing toward the presence or absence of competitive effects.

In introducing the Commentary, the Agencies first observe that the "vast majority of mergers pose no harm to consumers, and many produce efficiencies that benefit consumers in the form of lower prices, higher quality goods or services, or investments in innovation [that] enable companies to compete more effectively, both domestically and overseas." The Commentary then discusses each of first four analytical steps with illustrative enforcement examples, which provide valuable insights into the Agencies' thinking. (Issues concerning exiting and failing assets are not discussed in the Commentary "because those provisions are very infrequently applied.")

There are many notable points made in the 70-plus page Commentary. Among those concerning market definition, for example, are confirmation that the Agencies' definition of relevant antitrust markets do "not necessarily result in markets that include the full range of functional substitutes from which customers choose," and that customers typically are the best source, and in some cases the only source, of critical information concerning their ability and willingness to substitute in the event of a price increase, as well as that depending upon the competitive effects analysis, the consideration of multiple markets may be appropriate in a single deal.

Concerning competitive effects, the Agencies affirm their commitment to examining not only the price and output effects in the subject relevant markets, but also 'the effects of mergers in other dimensions of competition," such as in "innovation or some other form of non-price rivalry." As to unilateral effects in particular, among the observations are that "unilateral effects challenges . . . nearly always have involved combined shares greater than 35%," and that the merged firms "incentives" to raise price or reduce output are of paramount concern. As to coordinated effects, the Commentary provides that "likely coordination need not be perfect" but instead merely "sufficiently successful following the merger to result in anticompetitive effects," and that a "past history of coordination found unlawful can provide strong evidence of the potential for coordination after a merger," as well as that "if the acquired firm is a maverick, its acquisition may make coordination more likely."

The Agencies also observe that merger-related efficiencies may mitigate any such anticompetitive effects. Thus, the Commentary provides that "some mergers that appreciably reduce the uniformity of costs across competitors may disrupt existing coordination or otherwise make coordination less likely," and also that "sufficiently large reductions in the marginal costs of producing and selling the products of one or both of the merging firms may eliminate the unilateral incentive to raise prices that the merger might otherwise have created." The Agencies also note their consideration of "[e]fficiencies in the form of quality improvements," which also "may be sufficient to offset anticompetitive price increases following a merger." Additionally, the Agencies explain that they will seek to verify any claimed efficiencies by engaging in an assessment of the parties' analytical methods by reviewing the merging parties' internal documents and data, as well as the statements of knowledgeable company personnel.

Regarding entry analysis, the Commentary confirms that the "Agencies do not assess merely whether firms *could* commit incremental resources to the relevant market, but more importantly whether the proposed merger *would* be likely to induce firms to do so in a timely fashion and in a sufficient magnitude to deter or counteract the merger's anticompetitive effects," and thus the Agencies "focus on the sales opportunities created by the proposed merger." Additionally, the Commentary provides that "[s]uccessful prior entry can provide evidence that an anticompetitive merger would attract entry" but that "intellectual property rights such as patents can at times pose a significant entry obstacle."

These are but a sampling of the many observations made by the Agencies in the Commentary, which provides welcome guidance to counselors and companies alike.

For further information, please contact Steve Axinn at 212-728-2222, Pete Barile at 212-728-2215, or any other AVH attorney.