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DOJ and FTC release draft merger guidelines

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On July 19, 2023, the DOJ and FTC released a draft overhaul of the merger guidelines (the Draft Guidelines). Some portions of the Draft Guidelines are consistent with agency practice from prior administrations, but others set forth novel approaches that resemble stalled legislative reform priorities and theories of harm in court cases lost by the agencies. The weight courts will ultimately place on the guidelines, which lack the force of law and are not binding on courts, remains to be seen.

The public is invited to provide comments on the Draft Guidelines for a period of 60 days from release, or until September 18, 2023. The agencies state that they will use the public comments to evaluate and update the Draft Guidelines before finalizing them. Nevertheless, we expect that the finalized guidelines will remain substantially similar in approach to the Draft Guidelines.

But regardless of what the courts hold the law to be, the finalized guidelines will significantly influence how the FTC and DOJ conduct merger reviews and, as a result, the conduct and advocacy of potential merging parties. Thus, to the extent the Draft Guidelines set forth the agencies' approach to future transaction reviews, they are a strong indication of how the agencies may assess any particular deal. That view, in turn, has a substantial impact on how parties view antitrust transaction risks and sets expectations for what parties may encounter at the agency level before they ever reach court.

In some respects, the Draft Guidelines are consistent with the preceding guidelines and agency practice from prior administrations. But in other respects, the Draft Guidelines push merger review in novel directions or adopt key elements from a prior era of antitrust enforcement (i.e., the 1970s and earlier). Indeed, the majority of cases the Draft Guidelines cite for support predate 1980.

We outline here the most significant changes in the Draft Guidelines as compared to their predecessors and then summarize the full Draft Guidelines below:

- **Lower structural presumptions against transactions**. The Draft Guidelines restore the Herfindahl-Hirschman Index (HHI) thresholds for presumption of anticompetitive effects that prevailed prior to the 2010 Horizontal Merger Guidelines.
- **Unified guidelines for both horizontal and vertical transactions**. The Draft Guidelines eliminate the previous separate treatment of horizontal and vertical transactions in favor of a unified approach. Importantly, unlike the prior Vertical Merger Guidelines (issued during the Trump administration and withdrawn during the Biden administration), the Draft Guidelines do not entertain the notion that vertical transactions are inherently less problematic, nor do they acknowledge that there are certain well-established efficiencies to vertical transactions.
- **New structural presumption for vertical mergers**. Although the guidelines are now unified, the Draft Guidelines include a specific structural presumption of anticompetitive effect for vertical mergers that include a so-called "foreclosure share" of over 50% in a related upstream or downstream market to which rivals need access to compete.
- **Heightened importance of labor markets**. In one of their more controversial moves, the Draft Guidelines state that a transaction's effect on labor markets can be a stand-alone basis to challenge transactions. They further state that a

negative impact on labor markets cannot be overcome by citing to benefits in other markets.

- **New restrictions on firms with "dominant" positions**. The Draft Guidelines establish new structural presumptions against transactions involving firms with so-called "dominant" positions (meaning a market share of 30% or higher), regardless of whether other structural guardrails are triggered. More broadly, the Draft Guidelines state that transactions should not further "entrench or extend" a dominant position in the marketplace, which means that even an acquisition of a small player with minor share could come under scrutiny for a buyer with a 30% or higher share.
- **Heightened scrutiny of serial acquisitions or trends towards concentration**. Under the Draft Guidelines, the agencies assert a focus on concentration trends beyond what is presented in any particular transaction. Further, if a party is engaging in a series of transactions, the agencies may analyze the overall strategy of such acquisitions or look at them collectively.
- **Heightened scrutiny of transactions that eliminate potential entrants or perceived potential entrants**. The Draft Guidelines set forth certain structural criteria in which mergers involving potential entrants or, indeed, *perceived* potential entrants may be viewed as particularly problematic.

We now turn to a more comprehensive summary and assessment of the Draft Guidelines, noting where the Draft Guidelines diverge from the agencies' prior 2010 Horizontal Merger Guidelines (HMG), issued during the Obama administration, and the since-withdrawn 2020 Vertical Merger Guidelines (VMG), issued during the Trump administration.

Guideline-by-guideline summary

Guideline 1: Mergers should not significantly increase concentration in highly concentrated markets.

As with the 2010 HMG, the Draft Guidelines explain the relevance of market concentration to merger analysis and employ HHIs to measure concentration levels. The proposed treatment of market concentration differs, however, in two significant ways from the preceding HMG.

First, Guideline 1 sets forth a "structural presumption" that a merger will substantially lessen competition based on market structure alone. By contrast, the 2010 HMG merely referred to market concentration thresholds as a "useful indicator of likely competitive effects of a merger" and "not … a rigid screen."

In particular, Guideline 1 proposes that markets with a post-merger HHI greater than 1,800 are "highly concentrated"; if a merger results in a highly concentrated market and produces an increase in the HHI of more than 100 points, that merger is presumed to substantially lessen competition in violation of the antitrust laws. Alternatively, if a merger will result in a combined firm with a market share over 30% and an HHI increase of more than 100 points, that merger will also be presumed to substantially lessen competition regardless of overall market concentration. The Draft Guidelines refer to mergers that exceed the lowered concentration thresholds as "impermissible," leaving open the question of whether the agencies will view the structural presumption for such transactions as conclusive or rebuttable.

Second, the agencies propose to lower the concentration levels that warrant competitive concern, explaining that this change aligns the proposed Merger Guidelines with merger guidelines preceding the 2010 HMG. While the agencies now propose that markets with a post-merger HHI greater than 1,800 are "highly concentrated," the 2010 HMG defined highly concentrated markets as those with an HHI above 2,500. Similarly, the agencies suggest that markets with an HHI between 1,000 and 1,800 are "concentrated markets," while the 2010 HMG asserted that markets with an HHI below 1,500 were "unconcentrated."

Significantly, under the Draft Guidelines, firms that have significant, preexisting market shares or operate in markets with a limited number of players may find it more challenging to clear transactions at the agency and prior to litigation—even if the transaction involves a very small incremental change in market share.

Guideline 2: Mergers should not eliminate substantial competition between firms.

In addition to assessing market concentration, the agencies propose to review mergers for evidence of "substantial competition between the merger parties" as a means of determining whether a merger may substantially lessen competition. Guideline 2 is similar to the 2010 HMG, pursuant to which the agencies considered the extent to which merging parties were "substantial head-to-head competitors."

Guideline 3: Mergers should not increase the risk of coordination.

Guideline 3 states that the agencies will examine whether a merger increases the risk of anticompetitive coordination with respect to issues such as price, product features, customers, and wages. While similar guidance is found in the 2010 HMG, the Draft Guidelines go a step further by setting forth three circumstances under which the agencies will *presume* a merger may substantially lessen competition: (1) if the relevant market is "highly concentrated"; (2) if the market has seen prior anticompetitive coordination; or (3) if the merger eliminates a maverick firm, meaning a firm with a disruptive presence in the market, or changes its incentives. Similar to Guideline 1, Guideline 3 suggests that "dominant" firms or firms with a limited number of competitors may face increased difficulty in securing agency clearance of future mergers.

Guideline 4: Mergers should not eliminate a potential entrant in a concentrated market.

The 2010 HMG stated that mergers involving a "potential entrant can raise significant competitive concerns," but did not elaborate on the elements relevant to this issue. By contrast, Guideline 4 of the Draft Guidelines set forth that a "merger that eliminates a potential entrant into a concentrated market," i.e., a market with an HHI above 1,000, "can substantially lessen competition or tend to create a monopoly." The Draft Guidelines also state that, for mergers involving one or more potential entrants, "the higher the market concentration, the lower the probability of entry that gives rise to concern," and provide various factors relevant to whether a qualifying merger may substantially lessen competition.

Additionally, Guideline 4 suggests that a merger involving a *perceived* potential entrant (i.e., a firm perceived by the market as a potential entrant) can also substantially lessen competition and lists the factors relevant to the analysis of such mergers. Taking an apparently inconsistent position, however, the Draft Guidelines state that perceived potential entrants *cannot override or counteract harm* from mergers so as to be included in merging parties' entry-related rebuttals.

Guideline 5: Mergers should not substantially lessen competition by creating a firm that controls products or services that its rivals may use to compete.

Guideline 5 states that mergers may substantially lessen competition if they would allow a firm to control access to a product, service, or customers that its rivals use to compete. This determination is based on whether a firm has both the ability and incentive to make it harder for its rivals to compete in the relevant market (or to eliminate or deter new entrants). The agencies will also focus on whether mergers will result in a firm gaining access to a competitor's competitively sensitive information, which may undermine competition and/or facilitate coordination. In this regard, the agencies' stated competitive concerns are generally consistent with those stated in the now-withdrawn 2020 VMG.

In addition, the agencies will assess a firm's "ability" by determining the extent to which the firm can limit or degrade its rivals' access to a related product and affect those rivals' competitiveness. For example, higher prices paid by competitors might cause them to raise the prices they charge their customers, which makes that competitor's product less attractive to consumers.

The agencies will assess a firm's "incentive" based on the structure, history, and probable future of the market. The agencies will look at whether the firm has previously taken steps to limit rivals' access to the related product. The Draft Guidelines suggest that the agencies will look at internal documents for indications of incentive, but that documents showing procompetitive intent, or a lack of documents supporting anticompetitive intent, will not be dispositive. This is at odds with how courts have viewed such evidence in recent vertical cases, such as in the recent decision by the District Court of the Northern District of California denying the FTC's motion for a preliminary injunction in *FTC v. Microsoft*.[1] There, the court found persuasive the *lack* of evidence of an intent by the defendant to foreclose rivals.

Guideline 6: Vertical mergers should not create market structures that foreclose competition.

The agencies' stated primary concern with vertical mergers[2] is that companies may foreclose rivals from inputs or segments of the market otherwise open to them and thereby impair those rivals' ability to compete.

Guideline 6 diverges from the 2020 VMG by establishing a presumption that a "foreclosure share" (i.e., a merged party's share of a related upstream or downstream market) over 50% will substantially lessen competition. If the foreclosure share falls below the 50% threshold, the agencies will still examine a non-exhaustive list of "plus factors," including: (1)

the degree of integration between firms in the relevant and related markets and whether there is a trend towards further vertical integration; (2) whether the purpose of the merger is to foreclose rivals; (3) whether the relevant market is already concentrated; and (4) whether the merger increases barriers to entry by limiting independent sources of supply to potential new entrants.

Guideline 7: Mergers should not entrench or extend a dominant position.

Guideline 7 establishes a new structural presumption that a firm possessing at least 30% market share has a so-called "dominant" position (which is not consistent with some recent caselaw and appears to be more of a reflection of 1960s and 1970s-era jurisprudence). As set forth in Guideline 1, a firm with such a "dominant position" will confront a structural presumption of anticompetitive effects in any transaction involving more than a 100-point increase in HHI. Even if a firm's market share falls below that threshold, the agencies may still find that it has a dominant position if there is direct evidence that one or both merging firms has the power to raise price, reduce quality, or otherwise impose or obtain terms that they could not obtain but for that dominance.

If the agencies determine that a firm does have a dominant position, the analysis then shifts towards determining whether the merger would entrench that position. The agencies will consider whether the merger increases barriers to entry generally, increases switching costs, interferes with the use of competitive alternatives, deprives rivals of economies of scale or network effects, or eliminates a nascent competitive threat.

The Draft Guidelines assert that merger enforcement should not only prevent further concentration but also go further to "preserve the possibility of eventual deconcentration." As with many of the other Draft Guidelines, this guideline seeks to expand incipiency-based enforcement in a manner more consistent with earlier periods of antitrust jurisprudence.[3]

Guideline 8: Mergers should not further a trend toward concentration.

Guideline 8 states that a merger may substantially lessen competition if it contributes to a "trend toward concentration" and will examine two factors in making this assessment. *First*, the agencies will examine whether the merger is in a market or industry sector where there has been a significant tendency toward concentration.[4] *Second*, the agencies will examine whether the merger would increase the existing level of concentration or the pace of concentration.[5]

Guideline 9: When a merger is part of a series of multiple acquisitions, the agencies may examine the whole series.

Guideline 9 tracks the recent enforcement priority against so-called "serial acquisitions" positing that "[a] firm that engages in an anticompetitive pattern or strategy of multiple small acquisitions in the same or related business lines may violate Section 7, even if no single acquisition on its own would risk substantially lessening competition or tending to create a monopoly."[6] This guideline is consistent with prior scrutiny of sequential acquisitions by large companies, particularly those in the tech sector. Indeed, President Biden's 2021 executive order on competition specifically lists "serial mergers" as a cause of the rise of "dominant Internet platforms." This concept of an acquisition *strategy* violating the antitrust laws independent of any particular *merger* is not currently found in the 2010 HMG. More fundamentally, despite recent investigations into this area, we are not aware of any case that supports the proposition stated here.[7]

Guideline 10: When a merger involves a multi-sided platform, the agencies examine competition between platforms, on a platform, or to displace a platform.

Guideline 10 states that where a proposed transaction involves a platform operator, agencies will examine every aspect of platform competition, including "competition *between* platforms, competition *on* a platform, and competition to *displace* the platform." So long as a merger harms competition to "any group of participants" – i.e., around one side of the platform – regulators will seek to block the merger.[8] This is arguably a departure from the consumer welfare standard, as it suggests that harm to rival platforms and/or platform participants could cause the agency to block a transaction, even where consumers would benefit.

The Draft Guidelines also raise several possible theories that the agencies may consider in evaluating competition between, on, and to displace platforms, including network effects, foreclosing rival platforms and/or creating conflicts of interest, conglomerate acquisitions of services, or acquisitions of providers of key inputs (such as data). Beyond noting

possible theories and suggesting a special level of scrutiny of acquisitions by platform operators, the Draft Guidelines do not provide any specific, additional insight as to what acquisitions by a platform would give rise to a transaction that violates the antitrust laws under these theories.

Guideline 11: When a merger involves competing buyers, the agencies examine whether it may substantially lessen competition for workers or other sellers.

Guideline 11 notes that in addition to harm in consumer markets, the FTC will consider harm to buyer markets, including most importantly labor markets, largely using the same analysis as elsewhere. The Draft Guidelines highlight in particular that "reduction in labor market competition may lower wages or slow wage growth, worsen benefits or working conditions, or result in other degradations of workplace quality." The 2010 HMG similarly acknowledged that the agencies would evaluate whether a merger of two competitive buyers would lessen competition in a manner harmful to sellers, although it did not mention labor explicitly.

The Draft Guidelines go further than the 2010 HMG in explicitly stating that "[i]f the merger may substantially lessen competition or tend to create a monopoly in upstream markets, that loss of competition is not offset by purported benefits in a separate downstream product market." Importantly, that may mean that mergers that benefit consumers by lowering costs primarily through labor-related cost efficiencies may be deemed anticompetitive because of their impact on labor markets. If that is the approach taken by the agencies, it would be a notable departure from practice and materially change merger analysis. Notably, Commissioner Alvaro Bedoya focused heavily on the issue of labor markets in his statement released concurrently with the Draft Guidelines,[9] potentially suggesting the significance of this shift in how the agencies view labor market issues.

Guideline 12: When an acquisition involves partial ownership or minority interests, the agencies examine its impact on competition.

Tracking closely to Section 13 of the 2010 HMG, Guideline 12 notes that partial acquisitions may lessen competition to the extent that they give the partial owner the ability to influence the competitive conduct of the acquired firm, they reduce incentives to the acquiring firm to compete because they would otherwise benefit from the status quo, and to the extent that the partial acquisition would result in the sharing of non-public competitively sensitive information. We expect the agencies may draw upon this guideline in the context of acquisitions by private equity firms or other financial sponsors, which is a stated enforcement priority.

Guideline 13: Mergers should not otherwise substantially lessen competition or tend to create a monopoly.

Finally, Guideline 13 is a "catchall" that notes that the Draft Guidelines "are not exhaustive" and the agencies will consider other theories of anticompetitive harm. This is similar to the 2010 HMG, which similarly noted that the guidelines were not intended to be exhaustive.

Additional guidance

In addition to the 13 guidelines just discussed, the Draft Guidelines provide additional guidance on the tools the agencies use to define relevant markets and how the agencies consider rebuttal evidence showing that a merger does not substantially lessen competition. This guidance is summarized and evaluated below.

Market definition framework

The Draft Guidelines generally embrace more lenient standards for market definition than those contained in the 2010 HMG. While the Draft Guidelines, consistent with the 2010 HMG and applicable case law, provide that specific product market(s) and geographic market(s) must be analyzed, they emphasize that relevant markets "need not have precise metes and bounds" and note that defined product markets will be approximate, likely including some substitute products and omitting others. The Draft Guidelines no longer focus predominantly on the more-empirical Hypothetical Monopolist Test (HMT), but rather endorse more explicitly a broader set of qualitative information, such as observed market characteristics (or "practical indicia").

The Draft Guidelines also discuss three additional types of multi-product markets not delineated in the 2010 HMG: "cluster" markets, "bundled product" markets, and "one-stop shop" markets.[10] Although courts have recognized each of these types of market to some degree, the agencies' explicit discussion of these market forms appears consistent with its elevated attention in the Draft Guidelines to potential competitive harms from the extension of "dominant" positions to new markets, including by multi-product "platform" operators.

Rebuttal evidence showing that no substantial lessening of competition is threatened by the merger

Section IV of the Draft Guidelines discusses the evidence the agencies will consider in assessing whether specific market conditions and other procompetitive benefits neutralize or countervail the presumptions of anticompetitive effect. Specifically, the Draft Guidelines raise four possible types of rebuttal evidence:[11]

- **Failing firms**: This defense is generally disfavored and is rarely successful. The Draft Guidelines further cut this defense back, noting that the agencies will categorically reject arguments from parties that "a poor or weakening position should serve as a defense even when it does not meet [the required] elements."
- **Entry and repositioning**: Consistent with the 2010 HMG, the Draft Guidelines note that "the agencies assess whether entry induced by the merger would be 'timely, likely, and sufficient in its magnitude, character, and scope to deter or counteract the competitive effects of concern.'"[12]
- **Procompetitive efficiencies**: Consistent with the 2010 HMG, the Draft Guidelines note that "cognizable efficiencies must be of sufficient magnitude and likelihood that no substantial lessening of competition is threatened by the merger in any relevant market." The Draft Guidelines lay out four factors for determining whether an efficiency is cognizable:
  - **Merger specificity:** In a departure from the 2010 HMG, the Draft Guidelines appear to require consideration of all possible other alternatives, including "organic growth of one of the merging firms, contracts between them, mergers with others, or a partial merger involving only those assets." Indeed, it is difficult to imagine an efficiency that would not have some theoretical alternative.
  - **Verifiability:** Consistent with the 2010 HMG, the agencies will only credit efficiencies that can be verified by reliable methodology.
  - **Pass through to prevent a reduction in competition:** In what is an apparent new requirement, the Draft Guidelines require the merging parties to show how the efficiencies will improve competition within a short period of time. Implicitly, this requires showing a near-immediate increase in output or decrease in price.
  - **Procompetitive:** While framed as "procompetitive," this factor appears to be focused on harm to the "competitive process." Specifically, to be cognizable, these efficiencies cannot result from the "worsening of terms for the merged firm's trading partners," the "trend toward concentration," or "vertical integration." In particular, this suggests that the agencies will discount mergers that result in better products and cost savings from the elimination of double marginalization. In effect, the Draft Guidelines suggest that efficiencies that would otherwise benefit consumers will not be credited as "procompetitive" so long as they are inconsistent with how the agencies view a market should function.
- **Structural barriers to coordination unique to the industry**: The Draft Guidelines suggest that it is possible that "structural market barriers" may prevent anticompetitive coordination, but such conditions would be "exceedingly rare in the modern economy."

Practical implications

The Draft Guidelines in many key ways represent a substantial rewrite from previous merger guidelines. With that said, the Draft Guidelines also crystallize and codify the current thinking among leadership at the agencies as reflected in theories of harm fueling recent enforcement actions and will likely guide agency review of transactions in the near term. It remains to be seen how the judiciary will react to the positions set forth in the guidelines once finalized, though it should be noted that some of the theories set forth in the Draft Guidelines have already been rejected by courts in recent agency merger challenges. As noted, the Draft Guidelines rely heavily on dated jurisprudence from the 1960s and 1970s to the exclusion of more recent cases. To the extent that courts find the principles in the final guidelines unpersuasive or superseded by more recent law, the practical implications of the final guidelines may be less significant. Nevertheless, since the vast majority of merger reviews are resolved at the agency level (rather than in court), parties will need to consider shaping their advocacy to the agencies in ways that take into account the final guidelines.

If you have any questions regarding the matters covered in this publication, please reach out to any of the lawyers listed below or your usual Davis Polk contact.

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[1] *See* Davis Polk client update, *District court denies FTC's bid to halt Microsoft/Activision deal* (July 12, 2023), https://www.davispolk.com/insights/client-update/district-court-denies-ftcs-bid-halt-microsoftactivision-deal.

[2] A merger is "vertical" when the merging firms operate different levels of the same supply or distribution chain.

[3] *United States v. Phila. Nat'l Bank*, 374 U.S. 321, 365 n.42 (1963) ("[I]f concentration is already great, the importance of . . . preserving the possibility of eventual deconcentration is correspondingly great.").

[4] The agencies will look to market structure, with steadily increasing HHIs exceeding 1,000 and rising toward 1,800 establishing such a trend, or will look at other market characteristics, such as the exit of significant players. The lower HHI thresholds compared to the 2010 HMG could lead the agencies to assert upward concentration trends in markets previously regarded as unconcentrated.

[5] This may be established by a significant increase in concentration, such as a change in HHI greater than 200.

[6] In a footnote, the Draft Guidelines also note that such strategies may also violate Section 2 of the Sherman Act and Section 5 of the FTC Act.

[7] Consistent with that, the only case cited by the Draft Guidelines is *Brown Shoe*, which notes only that industry concentration is often the result of a cumulative series of mergers, not that the series of mergers itself would independently violate the antitrust laws.

[8] The Draft Guidelines except the "limited scenario of a 'special type of two-sided platform known as a transaction platform,'" which the Supreme Court considered in *American Express*, but argue that the requirement to consider all aspects of competition is limited to simultaneous transaction

platforms.

[9] Statement of Commissioner Alvaro M. Bedoya, July 19, 2023, https://www.ftc.gov/system/files/ftc_gov/pdf/p234000_merger_guidelines_statement_bedoya_final.pdf.

[10] These product markets comprise multiple, generally non-substitutable, products, whether because those products are each subject to similar competitive conditions (e.g., a "cluster" market of acute healthcare services provided by a hospital), because they are often sold in combination with one another (e.g., a "bundled product" market of multiple paper products), or because customers commonly purchase multiple products from a single supplier (e.g., a "one-stop shop" market of grocery stores).

[11] The Draft Guidelines also omit some mitigating or constraining factors noted in the 2010 HMG. In particular, the existing guidelines note that "[t]he agencies consider the possibility that powerful buyers may constrain the ability of the merging parties to raise prices."

[12] *Quoting FTC v. Sanford Health*, 926 F.3d 959, 965 (8th Cir. 2019).