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Three recent merger enforcement decisions signal challenges for U.S. antitrust agencies

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Under the Biden administration, the U.S. antitrust agencies are taking an aggressive approach to merger enforcement, and have outlined strategies that move away from historical merger review tools in favor of more enforcement-friendly standards. But recent court decisions have tested this new approach. Despite agency advocacy for novel theories, these decisions applied traditional legal analysis to find for the merging parties, questioning the agencies' ability to change merger review standards.

Three agency losses in September 2022

The Federal Trade Commission (FTC) recently challenged a vertical merger in the biotechnology sector and the Department of Justice (DOJ) challenged two mergers in the healthcare and agricultural sectors. In all three cases, the factfinder concluded that the agencies did not meet their legal burden to establish that the transactions were anticompetitive. We discuss the decisions below.

Illumina/GRAIL

On September 9, 2022, FTC Administrative Law Judge D. Michael Chappell (ALJ) issued a nearly 200-page decision dismissing the FTC's complaint against Illumina, Inc.'s vertical acquisition of GRAIL, Inc.

Illumina sells next-generation sequencing (NGS) instruments and consumables. GRAIL develops a blood-based multicancer detection (MCED) test that relies upon Illumina's NGS technology. GRAIL's product is the only NGS-based MCED test currently on the market in the United States. The FTC sued to block the transaction based upon a theory of vertical foreclosure—namely, that because Illumina is the dominant provider of a necessary input to MCED tests, the merged company would have the ability and incentive to harm GRAIL's rivals by withholding Illumina's NGS technology.

Before undertaking the transaction, Illumina publicized its willingness to offer a long-term, comprehensive supply agreement to all existing and new for-profit oncology customers who purchase its NGS products (the Open Offer). Illumina's Open Offer included provisions requiring Illumina to provide third-party customers equivalent (or superior) access to products and services as GRAIL receives, to offer customers grandfathered pricing terms, and to commit to enter into development agreements with customers and to supply them with new technology. Illumina also agreed to enter into a consent order with the FTC binding Illumina to the terms contained in the Open Offer. The Open Offer has a 12-year term, which the ALJ noted is consistent with what is typically provided in consent decrees that the FTC and DOJ have approved historically.[1]

The ALJ found that the FTC failed to prove its *prima facie* case of vertical foreclosure. In its post-trial brief, the FTC argued that it only needed to prove that Illumina has an ability and incentive to take action to harm GRAIL's *competitors*. The ALJ rejected this argument as a "minimalist formulation of the *prima facie* burden [which] is unsupported by applicable legal precedent."[2] In short, the ALJ found that the FTC had not established that harm to *rivals* equals harm to *competition*, as required by antitrust law.

The ALJ found that, even if harm to rivals was the appropriate standard, Illumina did not have the incentive to harm GRAIL's competitors. The ALJ found that the uncertainty of the future profitability of Illumina's clinical testing business and insufficient proof of diversion between GRAIL's MCED test and the MCED tests of GRAIL's purported rivals reduced the expected profitability of any foreclosure strategy Illumina might adopt.[3]

The ALJ also found that the evidence did not show that the acquisition would result in removing any NGS products from the market and, accordingly, would not likely lead to foreclosure. The ALJ found that the Open Offer would effectively constrain Illumina's ability to foreclose rivals. In so doing, the ALJ evaluated Illumina's economic incentives post-transaction. He gave weight to the public nature of the Open Offer, which led some Illumina customers to agree, or to say that they will agree, to the Open Offer. The ALJ found these facts to be significant in showing that the Open Offer was not illusory, unenforceable, or otherwise insufficient to prevent harm to rivals.

FTC staff has filed a notice to appeal the ALJ's decision to the full Commission.[4]

The parties have faced a different path so far in the European Union. Showing greater support for the FTC's theories, the European Commission (EC) held shortly thereafter, in a nonpublic decision, that Illumina would have both an ability and an incentive to harm GRAIL's rivals post-transaction and that the Open Offer remedy proposal did not adequately address the EC's competition concerns.[5] The parties are appealing an earlier decision regarding the EC's jurisdiction over this matter and are reported to be considering appealing this merits decision as well.

UnitedHealth/Change Healthcare

On September 19, 2022, Judge Carl Nichols of the U.S. District Court for the District of Columbia rejected the DOJ's bid to block UnitedHealth's acquisition of Change Healthcare. The transaction contained a horizontal overlap between the parties' claims-editing technology but was primarily a vertical transaction between the parties' businesses at different levels of the supply chain.

UnitedHealth is an integrated healthcare services provider and the owner of the largest commercial health insurer in the United States. UnitedHealth (through its subsidiary Optum) and Change Healthcare (through its ClaimsXten business) provide first-pass claims editing technology to health insurers in the United States, with an alleged combined market share of 90%. In addition, Change is a leading provider of electronic data interchange (EDI) clearinghouse services to health insurers, meaning that it has access to claims data of numerous health insurers, including competitors of UnitedHealth. The DOJ alleged that the transaction would give UnitedHealth access to rival health insurers' competitively sensitive information that UnitedHealth would use to gain an advantage and harm competition in health insurance markets (the "data-misuse" theory), and the ability and incentive to foreclose rivals' access to new EDI-related innovations, reducing competition in the health insurance market (the "foreclosure" theory).

With respect to the horizontal overlap, prior to litigation, the parties had proposed a full divestiture of Change's ClaimsXten business, which the DOJ rejected. The DOJ was not satisfied that the remedy would preserve the degree of competition that existed pre-transaction. The court held that the DOJ's standard was too stringent and that the appropriate legal standard is whether the transaction, including the divestiture, may lead to a substantial lessening of competition. The court also disagreed with the DOJ over the sufficiency of the divestiture buyer, finding that the ClaimsXten business was a highly separable asset that would retain its key employees and managers and that the divestiture buyer had significant experience with "carve-out investments" and the healthcare sector and "intends to invest substantially in the [divested] business."[6]

With respect to the vertical theories, the judge was broadly critical of the DOJ, stating that "the central problem with this vertical claim is that it rests on speculation rather than real-world evidence that events are likely to unfold as the Government predicts."[7] The court went on:

> [F]or it to be likely that the proposed acquisition would substantially lessen competition, United would have to uproot its entire business strategy and corporate culture; intentionally violate or repeal longstanding firewall policies; flout existing contractual commitments; and sacrifice significant financial and reputational interests. The Government has failed to show that United's post-merger incentives will lead it to take such extreme actions.[8]

As to the data-misuse theory, the court found that "Optum currently pursues a multi-payer business strategy, and the success of that strategy turns on payers and providers trusting that their data will be protected."[9] The court also credited the information firewalls and customer contract commitments that have been in place for years and that have protected rivals' data to date—facts the court noted were not rebutted by any witness for the DOJ.[10]

As to the foreclosure theory, the court similarly found that the DOJ had not provided real-world evidence that there would be actual harm, but instead was trying to "prove that United will likely withhold from its rivals products that don't even

exist."[11] The court found that the DOJ put forth no evidence that UnitedHealth had ever withheld products or provided third parties with a different product than provided to a UnitedHealth subsidiary (with the exception of products still in testing), which aligns with Optum's multi-payer business strategy, and that deviating from this strategy, and withholding products, would be harmful to the Optum business.

U.S. Sugar/Imperial Sugar

On September 23, 2022, Judge Maryellen Noreika of the U.S. District Court for the District of Delaware rejected the DOJ's attempt to block U.S. Sugar Corp.'s acquisition of Imperial Sugar. The litigation, brought in November 2021, was the DOJ's first merger challenge under the Antitrust Division's current Assistant Attorney General (AAG) Jonathan Kanter. The DOJ has announced its intention to appeal Judge Noreika's decision.

In seeking to block the transaction, the DOJ advanced a generally conventional horizontal theory of harm in an alleged relevant market for the production and sale of refined sugar to wholesale customers in (1) the Southeast United States and (2) Georgia.[12] U.S. Sugar owns United Sugar, a cooperative of four sugar producers in the United States. After the acquisition, Imperial Sugar would join this cooperative. The DOJ alleged that the transaction would result in United Sugar accounting for 42% of sales in the Southeast United States and United Sugar and its largest remaining rival, Domino, accounting for 75% of sales in the Southeast United States.[13] The DOJ alleged these asserted market conditions presented a "straightforward" case that the transaction would substantially lessen competition.[14]

The court found that the DOJ failed to establish a *prima facie* case that the transaction would substantially reduce competition. In its decision, the court focused primarily on flaws in the DOJ's alleged relevant markets, which the court found to "ignore the commercial realities of sugar supply in the U.S."[15] The court found several facts in support of this holding, including the DOJ's failure to prove that sugar distributors did not compete with sugar producers for the sale of refined sugar,[16] the DOJ's unproven assumption that all "wholesale" customers constituted a single market,[17] and the DOJ's failure to account for the national sourcing behavior of customers in the DOJ's alleged geographic markets.[18] The court also found the U.S. Department of Agriculture's "intimate involvement" with the U.S. sugar industry, and its ability to regulate the sugar supply to reduce prices, would mitigate any potential harm to sugar consumers from the transaction.[19]

The impact of recent losses on agency enforcement priorities

The DOJ and FTC are not without victories in their recent merger enforcement efforts. In the last year, agency opposition has caused parties to abandon a number of deals, including Lockheed Martin's proposed acquisition of Aerojet and Nvidia's proposed acquisition of ARM. In addition, a number of high-profile merger challenges in a variety of industries, including publishing, virtual reality, and door locks, have yet to be resolved.

Moreover, in recent congressional testimony, AAG Kanter and FTC Chair Lina M. Khan have reaffirmed their commitment to aggressive merger (and non-merger) enforcement. AAG Kanter strongly asserted to Congress that "[i]mprovements to antitrust enforcement will not happen if the Antitrust Division is unwilling to challenge aggressively anticompetitive conduct and unlawful market consolidation. I am committed to bringing difficult cases, and as I have mentioned, the Antitrust Division is building a team of litigators that are ready for the challenge."[20] Similarly, FTC Chair Khan stated that "[t]he Commission will not hesitate to identify and impose broad relief to protect Americans and deter illegal activity now and in the future."[21]

Nevertheless, recent agency losses raise questions about FTC and DOJ leadership's ability to implement their aggressive enforcement agenda, particularly as it relates to nontraditional theories of harm. Moreover, current leadership appears to favor injunctive relief over negotiated remedies. As discussed below, both efforts become more difficult when courts hold the agencies to established legal standards.

Vertical merger enforcement and revisions to the merger guidelines

Aggressive vertical merger enforcement is a central tenet of current FTC and DOJ leadership. We expect this principle to be reflected in updated agency merger guidelines. The agencies have stated that the prior Vertical Merger Guidelines were "flawed," and that vertical merger enforcement to date has been too narrowly focused.[22] FTC Chair Khan has recently stated the agencies' objective as "captur[ing] the full set of ways in which mergers can harm competition," and said that "[c]entral to this effort is placing greater weight on assessing both non-horizontal and forward-looking competitive harm."[23] The FTC has stated that it is "reorienting [its] enforcement efforts to better capture harm from mergers involving firms at different levels of the supply chain (i.e., non-horizontal mergers) and to better anticipate future

competition concerns before markets are dominated by only a few firms," an "approach [that] is being incorporated into FTC merger review generally and has been reflected in several recent merger challenges."[24]

The DOJ has expressed a similar sentiment: "Too often, we have treated the test for illegality as essentially a rule of reason balancing framework, limited to models that attempt to concretely predict the precise effects of a merger on prices. But this leaves underenforced a statute that was meant to be prophylactic."[25] In short, the FTC and DOJ see prior merger enforcement as being too focused on actual effects and, therefore, too restrictive on the agencies' enforcement activities.

In *Illumina/GRAIL* and *UnitedHealth/Change Healthcare*, the agencies' cases focused on the theoretical incentives that the vertically-merged companies might have post-transaction. In each case, however, the factfinder rejected those theories in the face of inconsistent real-world evidence. The decisions in these proceedings also indicate skepticism of the agencies' theories as a matter of law. The ALJ's decision in *Illumina/GRAIL* in particular can be read as a rebuke to the FTC's attempts to bring enforcement actions under expansive readings of the law. There, the ALJ held that "[e]conomic theories about incentive are largely irrelevant absent a meaningful ability to act on it," and that "theory and speculation cannot trump facts."[26] It remains to be seen whether the agencies will revise their enforcement theories in light of these decisions.

The *U.S. Sugar/Imperial Sugar* decision suggests that courts deciding challenges to horizontal mergers will also continue to favor concrete factual and economic evidence when it comes to both market definition and theories of harm. Several pending cases present important tests for horizontal merger enforcement and the scope of theories and evidence that courts will find persuasive.

Favoring injunctive relief over merger remedies

FTC and DOJ leadership also have expressed greater skepticism toward settlements with merging parties. As discussed above, even after the ALJ found that Illumina's Open Offer—which Illumina agreed to incorporate into an FTC consent order—was an important factor that would have constrained the alleged anticompetitive harm in the merger, FTC Chair Khan has continued to assert that the FTC "strongly disfavor[s] behavioral remedies and will not hesitate to reject proposed divestitures that cannot fully cure the underlying harm."[27] AAG Kanter has also stated that he is "concerned that merger remedies short of blocking a transaction too often miss the mark" and that "[c]omplex settlements, whether behavioral or structural, suffer from significant deficiencies."[28] In September, AAG Kanter went so far as to say that "[o]ne of [his] highest priorities was to increase the Division's capacity to block more illegal mergers."[29]

In *UnitedHealth/Change*, however, the district court confirmed that structural remedies (i.e., divestitures) can adequately address competitive concerns and rejected the agencies' aversion to PE firms as suitable purchasers. In *Illumina/GRAIL*, the ALJ's decision that the transaction would not harm competition relied heavily on the Open Offer's ability to prevent the occurrence of the FTC's alleged harms, because it included a range of terms that addressed the theoretical areas of foreclosure and included monitoring and enforcement provisions. Both purported "fixes" reflect a similar decision by the merging parties in *AT&T/Time Warner*, who created a commercial "fix" to respond to the DOJ's concerns and then litigated that fix successfully, resulting in a DOJ loss at trial. These decisions indicate that transacting parties should continue to seek "fix-it-first" commercial solutions or remedies where plausible.

Key takeaways

Under the Biden administration, FTC and DOJ leadership have outlined aggressive merger enforcement agendas. In three recent decisions, however, the FTC's ALJ and district court judges have held the agencies to established precedent on enforcement standards, rejecting the agencies' attempts to seek lower legal thresholds for anticompetitive behavior.

But there is no sign that the FTC or DOJ are backing off and a number of high-profile merger challenges remain undecided. It is therefore likely that there will be more litigated mergers in the coming year. Parties contemplating transactions that raise potential antitrust issues should carefully consider whether there are ways to address competition issues proactively up front and whether they are prepared to take the deal to litigation if they encounter entrenched opposition.

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1 *Illumina, Inc. and GRAIL, Inc.*, No. 9401 (Sept. 9, 2022) (Initial Decision), at 121.

2 *Id*. at 168.

3 *Id*. at 172-78.

4 Complaint Counsel's Notice of Appeal, *Illumina, Inc. and GRAIL, Inc.*, No. 9401 (Sept. 2, 2022).

5 *Mergers: Commission Prohibits Acquisition of GRAIL by Illumina*, European Commission (Sept. 6, 2022), https://ec.europa.eu/commission/presscorner/detail/en/ip_22_5364.

6 *United States v. UnitedHealth Group, Inc., et al.*, No. 1:22-cv-0481 (CJN), 2022 WL 4365867, at *11–*12 (D.D.C. Sept. 19, 2022).

7 *Id.* at *16.

8 *Id.*

9 *Id.* at *19.

10 *Id.*

[11] *Id.* at *26.

[12] Complaint, *United States v. United States Sugar Corp., et al.*, No. 1:21-cv-01644-UNA (D. Del. Nov. 23, 2021), at ¶ 26.

[13] *Id*. at ¶ 4.

[14] *Id*. at 2.

[15] *United States v. United States Sugar Corp., et al.*, No. 1:21-cv-01644-UNA (D. Del. Nov. 23, 2021), at 41.

[16] *Id*. at 44.

[17] *Id*. at 48.

[18] *Id*. at 51.

[19] *Id*. at 55.

[20] Assistant Attorney General Jonathan Kanter of the Antitrust Division Testifies Before the Senate Judiciary Committee Hearing on Competition Policy, Antitrust, and Consumer Rights (Sept. 20, 2022), https://www.justice.gov/opa/speech/assistant-attorney-general-jonathan-kanter-antitrust-division-testifies-senate-judiciary.

[21] Lina M. Khan, Chairwoman, Federal Trade Commission, Prepared Statement of the Federal Trade Commission Before the United States Senate Committee on the Judiciary Subcommittee on Antitrust, Competition Policy and Consumer Rights, Oversight of the Enforcement of the Antitrust Laws, at 5 (Sept. 20, 2022), https://www.ftc.gov/system/files/ftc_gov/pdf/P210100SenateAntitrustTestimony09202022.pdf.

[22] *Federal Trade Commission Withdraws Vertical Merger Guidelines and Commentary*, Federal Trade Commission (Sept. 15, 2021), https://www.ftc.gov/news-events/news/press-releases/2021/09/federal-trade-commission-withdraws-vertical-merger-guidelines-commentary.

[23] Lina M. Khan, Chairwoman, Federal Trade Commission, Prepared Statement of the Federal Trade Commission Before the United States Senate Committee on the Judiciary Subcommittee on Antitrust, Competition Policy and Consumer Rights, Oversight of the Enforcement of the Antitrust Laws, at 5 (Sept. 20, 2022), https://www.ftc.gov/system/files/ftc_gov/pdf/P210100SenateAntitrustTestimony09202022.pdf.

[24] *Id*. at 2, 5.

[25] Jonathan Kanter, Assistant Attorney General, Antitrust Division, Department of Justice, Respecting the Antitrust Laws and Reflecting Market Realities (Sept. 13, 2022), https://www.justice.gov/opa/speech/assistant-attorney-general-jonathan-kanter-delivers-keynote-speech-georgetown-antitrust.

[26] *Illumina, Inc. and GRAIL, Inc.*, No. 9401 (Sept. 9, 2022) (Initial Decision), at 197.

[27] Lina M. Khan, Chairwoman, Federal Trade Commission, Prepared Statement of the Federal Trade Commission Before the United States Senate Committee on the Judiciary Subcommittee on Antitrust, Competition Policy and Consumer Rights, Oversight of the Enforcement of the Antitrust Laws, at 6 (Sept. 20, 2022), https://www.ftc.gov/system/files/ftc_gov/pdf/P210100SenateAntitrustTestimony09202022.pdf.

[28] Assistant Attorney General Jonathan Kanter of the Antitrust Division Delivers Remarks to the New York State Bar Association Antitrust Section (Jan. 24, 2022), https://www.justice.gov/opa/speech/assistant-attorney-general-jonathan-kanter-antitrust-division-delivers-remarks-new-york.

[29] Assistant Attorney General Jonathan Kanter of the Antitrust Division Testifies Before the Senate Judiciary Committee Hearing on Competition Policy, Antitrust, and Consumer Rights (Sept. 20, 2022), https://www.justice.gov/opa/speech/assistant-attorney-general-jonathan-kanter-antitrust-division-testifies-senate-judiciary.