

**MERGERS AND ACQUISITIONS:
UNITED STATES GOVERNMENT ANTITRUST
ANALYSIS AND ENFORCEMENT**

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INTRODUCTION

In the field of mergers, the Federal Trade Commission (FTC) and the Antitrust Division of the Department of Justice (DOJ) (hereinafter “Agencies”), along with the state Attorneys General, continue to vigorously investigate transactions with potential anticompetitive effects and pursue enforcement action in such cases. This paper overviews the U.S. merger analysis process and examines the basic components of merger analysis, highlighting some of the more significant aspects of the Merger Guidelines such as Market Definition and Measurement, Market Shares and Concentration, Competitive Effects, Entry, Efficiencies, and Failure and Exiting Assets. The paper then examines some of the Agencies’ notable 2003 activities and briefly describes other developments in the DOJ’s and FTC’s review of the premerger and merger processes.

I. U.S. MERGER ANALYSIS OVERVIEW

The 1992 U.S. Government Merger Guidelines¹ (“Guidelines”) articulate the basic approach taken by U.S. enforcement agencies to antitrust merger analysis. The Hart-Scott-Rodino Act (“HSR”)² requires that parties to a proposed merger provide pre-merger notification

¹ U.S. Department of Justice and Federal Trade Commission Horizontal Merger Guidelines (issued Apr. 2, 1992, revised April 8, 1997), *reprinted in* 4 TRADE REG. REP. (CCH) ¶ 13,104 (“Merger Guidelines”).

² Hart-Scott-Rodino Antitrust Improvements Act of 1976, Clayton Act § 7A, 15 U.S.C. § 18a (Mar. 11, 2003). *See also* Federal Trade Commission regulations under HSR, 16 C.F.R. §§ 801, *et. seq.* (April 1, 2003).

to the FTC and the Antitrust Division of the DOJ (the “Agencies”) if the size of the transaction and parties exceeds certain thresholds.

Generally speaking, HSR requires both the acquiring and acquired entities to file notifications under the program if all of the following conditions are met:

- (1) One entity has sales or assets of at least \$100 million,
- (2) The other entity has sales or assets of at least \$10 million,
- (3) As a result of the transaction, the acquiring entity will hold an aggregate amount of stock and assets of the acquired person either:
 - a. valued at more than \$50 million; or
 - b. valued at more than \$200 million, regardless of the sales or assets of the acquiring and acquired persons.³

HSR applies to mergers, consolidations, tender offers, private purchases, acquisitions of assets and other acquisitions of voting securities, as well as to the formation of joint ventures in corporate form.⁴ Special rules apply to acquisitions by partnerships.⁵

The Agencies analyze all transactions reported under HSR in order to determine whether enforcement action is warranted. Generally, the federal agencies will review mergers, acquisitions and joint ventures to determine whether they violate Section 7 of the Clayton Act, which prohibits a corporation “engaged in commerce” from acquiring the stock or share capital or assets of another corporation where the effect of the acquisition “may be substantially to lessen competition, or to tend to create a monopoly.”⁶ Thus, Section 7 authorizes the Government and others to challenge a merger or acquisition in its incipiency if the transaction is likely to lessen competition substantially or to create a monopoly. More specifically, “Section 7 does not require proof that a merger or other acquisition has caused higher prices in the affected market. All that is necessary is that the merger create an appreciable danger of such

³ *Id.*

⁴ *Id.*

⁵ *Id.*

⁶ 15 U.S.C. § 18 (2003).

consequences in the future. A predictive judgment, necessarily probabilistic and judgmental rather than demonstrable . . . is called for.”⁷

To predict whether an acquisition may substantially lessen competition or tend to create a monopoly, the reviewing court must determine: (1) the line of commerce or product market in which to assess the transaction; (2) the geographic market in which to assess the transaction; and (3) the transaction’s probable effect on competition in the product and geographic markets.⁸ If the challenged acquisition would result in the creation or enhancement of market power, defined as the ability profitably to raise price above a competitive level for a period of time, then competition would be adversely affected.

While Section 7 of the Clayton Act is the principal statute concerned with mergers, Sections 1 and 2 of the Sherman Act⁹ and Section 5 of the FTC Act may also be implicated.¹⁰

The Guidelines are the Government’s major analytical framework for determining when an acquisition may substantially lessen competition or tend to create a monopoly in violation of Section 7; they are not, however, binding on the courts.¹¹

The Guidelines represent a significant milestone in coordination and cooperation between the Department of Justice and the Federal Trade Commission, which share responsibility for enforcing the federal antitrust laws. The Guidelines represent an evolutionary development, building on the basic principles of the 1982 and 1984 Merger Guidelines and the Commission’s 1982 Statement Concerning Horizontal Mergers.

This paper touches briefly on the 1992 Guidelines’ overview section and then examines the basic components of merger analysis. The paper does not attempt to discuss every aspect of merger analysis but instead highlights some of the more significant aspects of the Guidelines.

A. **Purpose, Underlying Policy Assumptions and Overview**

⁷ Hospital Corp. of Am. v. FTC, 807 F.2d 1381, 1389 (7th Cir. 1986) (citing United States v. Phila. Nat’l Bank, 374 U.S. 321, 362 (1963)).

⁸ United States v. Marine Bancorporation, 418 U.S. 602, 618 – 23 (1974).

⁹ 15 U.S.C. §§ 1, 2 (2003).

¹⁰ 15 U.S.C. § 45(a)(1) (2003). Section 5 of the FTC Act prohibits unfair or deceptive acts or practices in or affecting commerce. The Commission will find deception if there is a representation, omission, or practice that is likely to mislead the consumer acting reasonably in the circumstances, to the consumer’s detriment. FTC POLICY STATEMENT ON DECEPTION, 103 F.T.C. 110, 174 (1984).

¹¹ See, e.g., Olin v. FTC, 986 F.2d 1295, 1300 (9th Cir. 1993) (stating that “[c]ertainly the [Merger] Guidelines are not binding on the courts, or, for that matter, on the [Federal Trade] Commission.” (citations omitted)).

The primary objective of U.S. merger analysis is to identify mergers that are likely to create or enhance market power. “The process of assessing market concentration, potential adverse competitive effects, entry, efficiency and failure is a tool that allows the Agency to answer the ultimate inquiry in merger analysis: whether the merger is likely to create or enhance market power or to facilitate its exercise.”¹²

The Guidelines set forth a five-step assessment of mergers: (1) market definition, measurement and concentration; (2) the potential adverse competitive effects of mergers; (3) entry; (4) efficiencies; and (5) failure.¹³ The Agencies will also consider, *inter alia*, direct evidence that a merger will have anticompetitive effects. Examples of this type of direct evidence include the merging parties’ internal documents or the statements of customers predicting a supracompetitive price increase.

B. Market Definition and Measurement

When evaluating a merger under the Guidelines, the initial task is to determine the relevant product and geographic markets, and assess the change in market structure that the merger will likely cause. A product market is defined by including all products that, from a consumer-demand perspective, are reasonable substitutes for the relevant product.¹⁴ According to the Guidelines, such a determination is made by including all products to which consumers would switch in the face of a small but significant non-transitory price increase (“SSNIP”).¹⁵

The Guidelines also preserve the Agencies’ flexibility to consider hypothetical price increases of either larger or smaller than five percent, where appropriate, given the nature of the industry.¹⁶ In particular, if “premerger circumstances are strongly suggestive of coordinated

¹² Merger Guidelines, § 0.2.

¹³ *Id.*

¹⁴ *Id.* at § 1.12.

¹⁵ *Id.*

¹⁶ *Id.* The Guidelines directly confront the so-called “Cellophane” trap, which refers to the error many people believe the Supreme Court committed in the *Du Pont* decision. *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377 (1956). There, the Court held that Du Pont did not have market power because there were good substitutes for its product, cellophane, at prevailing market prices. But *Du Pont* critics claim that the Court did not consider the apparent fact that Du Pont was *already* exercising market power, raising cellophane prices above competitive levels and bringing it into competition with higher-priced substitutes. Lawyers and economists have debated whether the pre-revision Guidelines permitted users to fall into the Cellophane trap, but the post-revision Guidelines should end the debate.

interaction,”¹⁷ then the Agencies “will use a price more reflective of the competitive price”¹⁸ rather than using pre-merger prices as the base to which a hypothetical increase will be added.¹⁹

When defining a particular product market, the Guidelines also include firms that likely would enter the relevant market “within one year and without the expenditure of significant sunk costs of entry and exit” in response to a SSNIP.²⁰ The Guidelines term these firms “uncommitted entrants” because the firms could quickly cease production without significant loss; their presence likely influences the market both before and after the merger.²¹ Sunk costs are market-specific investments in assets that cannot be recovered through redeployment outside the relevant market; a “significant” sunk cost is defined as one that would not be recouped within one year.²²

The overall approach to market definition is consistent with the Guidelines’ underlying premises in focusing on the ability of sellers to raise prices profitably after the merger. In accordance with the Guidelines approach, alternatives to which consumers can turn in the face of a price increase, either in terms of products or suppliers, must be included in the relevant markets in which the competitive effects of the merger are being evaluated, if the products or suppliers constrain the ability of the merged firms and its competitors to raise prices.

C. Market Shares and Concentration

Once the relevant market is determined, the next step of merger analysis is to assess the potential transaction’s impact on concentration in the relevant markets. In 1982, the four-firm concentration ratio gave way to the Herfindahl-Hirschman Index (“HHI”), which is generally considered a more accurate measure of competitive conditions in a market. The HHI captures both the number of firms in an industry and their relative sizes.²³ The Guidelines view

¹⁷ Merger Guidelines, § 1.11.

¹⁸ *Id.*

¹⁹ *Id.*

²⁰ *Id.* at § 1.32. *See also id.* at § 1.321.

²¹ The Guidelines note that if such “uncommitted” entrants “would also remain in the market and would meet” the tests for entry set forth in Section 3, they will be considered in the entry analysis. *Id.* at § 1.32 n.13.

²² *Id.* at § 1.32. The Guidelines balance specificity in the market definition analysis with an acknowledgment of the need for flexibility in carrying out the analysis. For example, they point out that because precisely calculating sunk costs may be difficult, the Agencies will, when necessary, “make an overall assessment of the extent of sunk costs for firms likely to participate through supply responses.” *Id.*

²³ The HHI is calculated by squaring the percentage market share of each firm in the market and then adding those squares. Most antitrust practitioners believe that the HHI is generally a more accurate measure of

concentration as the best threshold indicator of the potential competitive impact of a merger because the risk of the exercise of market power increases as markets become significantly more concentrated. Even though concentration is a key factor in assessing a market's future competition, it may be outweighed if other conditions in the market clearly make the exercise of market power unlikely.

Under the Guidelines, when a merger would increase the HHI by more than 100 points to a post-merger HHI exceeding 1800, "it will be presumed that . . . [such merger is] likely to create or enhance market power or facilitate its exercise."²⁴ This presumption of illegality "may be overcome" by a showing that other factors in the Guidelines' analysis make anticompetitive effects unlikely.²⁵ Mergers producing an HHI increase of more than 100 in moderately concentrated (1000-1800 HHI) markets potentially raise significant competitive concerns, depending on the analysis of other market factors.²⁶

As a theoretical matter, other things being equal, both coordinated interaction and the unilateral exercise of market power tend to become more likely as concentration levels increase and the number of firms in the market decreases. As a practical matter, the higher the post-merger concentration, the more important it is for the rebuttal case to be sound. Even a merger to monopoly may be allowed to proceed if entry is sure to be timely, likely, and sufficient to deter or counteract any anticompetitive effects.²⁷

The Guidelines incorporate this principle. When a merger leads to market concentration above 1800 HHI, the requisite showing that other factors make the presumed anticompetitive effects unlikely is not evaluated in a vacuum, but "in light of market concentration and market shares."²⁸ As market concentration increases significantly above 1800 HHI, the showing must be better supported by the evidence. Moreover, the Guidelines expressly recognize that "[o]ther things being equal, market concentration affects the likelihood that one firm, or a small

market concentration than two-firm or four-firm concentration ratios because it takes into account both the number and size distribution of all sellers in a market. The change in concentration caused by a merger is calculated by subtracting the HHI based on the premerger market shares from the HHI based on the post-merger market shares.

²⁴ Merger Guidelines, § 1.51(c).

²⁵ *Id.*

²⁶ *Id.* at § 1.51(b).

²⁷ See generally Janusz A. Ordover and Jonathan B. Baker, *Entry Analysis Under the 1992 Horizontal Merger Guidelines*, 61 ANTITRUST L.J. 139 (1992).

²⁸ Merger Guidelines, § 1.51(c).

group of firms, could successfully exercise market power” either unilaterally or through coordination.²⁹

One must be careful in that acknowledging the existence of a relationship between concentration and likely competitive effects is not to assume that there is a precise mathematical relationship between the two. Extended focus on relatively minor differences in concentration statistics “suggests that the numbers have a scientific predictive value that does not exist.”³⁰

D. Competitive Effects

Section 2 of the Guidelines describes in greater detail the manner in which mergers may lead to higher prices or the loss of other forms of competition, especially unilateral and coordinated potential competitive effects. For example, through tacit or express coordination, firms may pursue strategies that are harmful to consumers and that are profitable for each firm only because of the other competitors’ accommodating reactions. In its simplest manifestation, coordination may entail a decision to follow an unjustified price increase initiated by the market leader rather than maintaining current prices and battling for an increased market share. According to the Guidelines, coordination need not involve “complex terms”³¹ but “may, instead, follow simple terms such as a common price, fixed price differentials, stable market shares, or customer or territorial restrictions.”³²

The Guidelines further explain that successful coordinated interaction entails (1) reaching terms of coordination that are profitable to the firms involved; (2) the ability to detect deviations from those terms; and (3) the ability to punish such deviations.³³ The importance of detection and punishment derives from the inherent stability of cartels. It is usually more profitable for a firm to cheat on a cartel agreement than to abide by the agreement, as long as the firm is not caught and punished. Successful coordination requires that deviations from any terms of coordination be detectable and punishable, so that coordinating firms find it in their interests to abide by the terms of coordination rather than deviate from them. Thus, the

²⁹ *Id.* at § 2.0. *See, e.g.,* United States v. Baker Hughes Inc., 908 F.2d 981, 990-91 (D.C. Cir. 1990) (holding that under Section 7 of the Clayton Act, market share data establishes the Government’s prima facie case, shifting the burden to the defendant to “rebut [the] presumption of anticompetitive effect [and] show that the prima facie case inaccurately predicts the relevant transaction’s probable effect on future competition. . . . The more compelling the prima facie case, the more evidence the defendant must present to rebut it successfully”). The government retains the ultimate burden of persuasion. *Id.* at 983. For an extended discussion, *see In re B.F. Goodrich Co.*, 110 F.T.C. 207, 305, 338-39 (1988).

³⁰ *Id.* at 355 (Azcuena, Commissioner, concurring in part and dissenting in part).

³¹ Merger Guidelines, § 2.11.

³² *Id.*

³³ *Id.* at § 2.1.

Guidelines state that an effective collusive scheme requires that deviations or “cheating” be deterred by a credible threat of punishment, and credible punishment “may not need to be any more complex than temporary abandonment of the terms of coordination by other firms in the market.”³⁴

Under the Guidelines, the working presumption continues to be that if the post-merger HHI exceeds 1800, then the market is prone to coordination.³⁵ However, the Guidelines call upon the Agencies to carefully examine available evidence concerning the extent to which market conditions are conducive to reaching terms of coordination and to detecting and punishing deviations in order to determine whether this presumption has been overcome.³⁶

In addition to reducing competition through coordinated interaction, the Guidelines also recognize that a post-merger firm may find it profitable to unilaterally raise prices and suppress output.³⁷ Two theories of unilateral anticompetitive harm are set forth.

The first theory considers a market for differentiated products, in which buyers regard the products of the merged entities as particularly close substitutes for one another. If the merged entity raises the price of product A, some of the sales loss due to the price rise would be diverted to the company’s newly acquired product line, product B. “[C]apturing such sales loss through merger may make the price increase profitable even though it would not have been profitable premerger.”³⁸ The anticompetitive effect falls upon the buyers who regard the merging firms’ products as particularly close substitutes. This strategy does not require the cooperation of rivals.

The second theory relates to markets in which products are relatively undifferentiated and firms are primarily distinguished by capacity, which also shapes the nature of their competition. Suppose that a merger creates a firm with a substantial market share, competitors are already producing at or near their capacity, and expanding capacity is difficult. The newly formed firm may find it profitable to raise its prices and reduce joint output unilaterally because the lost revenues on the foregone sales may be outweighed by the resulting price increase on the remaining sales (along with the cost reductions associated with decreased output). The

³⁴ *Id.* at § 2.12. Note, however, that while the three inquiries discussed above are conceptually separate, in a particular case the same evidence may be relevant to more than one conceptual category. “Certain market conditions that are conducive to reaching terms of coordination also may be conducive to detecting or punishing deviations from those terms.” *Id.* at § 2.1. Examples include product homogeneity and availability of price information.

³⁵ *See id.* § at 1.51.

³⁶ *See generally id.* at § 2.

³⁷ *Id.* at § 2.22.

³⁸ *Id.* at § 2.21.

Guidelines point out that this may be the case even if the merged firms' combined market share is lower than what might colloquially be thought of as a "monopoly" share.³⁹

E. Entry

Entry has become one of the most hotly contested issues in U.S. merger cases. It is, however, often treated in isolation from its likely impact on behavior in the market under scrutiny. The Guidelines put entry analysis into the context of assessing the merger's impact on competition.

According to the Guidelines, the relevant inquiry is whether entry "would deter or counteract" the merger's anticompetitive effects.⁴⁰ The first question is whether entry would be timely, which generally means that it "can be achieved within two years from initial planning to significant market impact."⁴¹ All phases of entry will be included in this calculation.⁴² This requires a realistic assessment that goes beyond, for example, the time needed to construct a plant and looks at front- and back-end steps that the entrant must accomplish in order to have a significant impact on the market.

The second question is whether entry is likely, meaning it would be profitable at premerger prices and such prices could be secured by the entrant.⁴³

The third question is whether entry would be sufficient to counteract the merger's potential anticompetitive effects.⁴⁴ When the tangible and intangible assets needed for entry are readily available and entry is found to be both timely and likely, then sufficiency is also ordinarily found.⁴⁵

F. Efficiencies

³⁹ *Id.* at § 2.22.

⁴⁰ *Id.* at §§ 3.0, 3.2.

⁴¹ *Id.* at § 3.2.

⁴² Entry phases may include planning, design, management, permitting, licensing and other approvals, construction, debugging, promotion, marketing, distribution and satisfaction of customer testing and qualification requirements. *Id.* at § 3.1.

⁴³ *Id.* at § 3.3.

⁴⁴ *Id.* at § 3.4.

⁴⁵ *Id.*

It is widely recognized that mergers can enhance efficiency and thereby lower the costs of production and benefit consumers. Efficiencies generated by a merger may, among several other factors, cause the Agencies to conclude that a transaction, on balance, will be beneficial rather than harmful to competition.

Even when a merger otherwise appears to threaten competition by further exacerbating an already concentrated market, and those concerns are not eliminated by ease of entry or other market conditions, the merger may result in such substantial efficiency savings – which could not be captured in any other way – that the transaction on balance may be deemed to be procompetitive.

In April 1997, the Agencies revised the Guidelines to clarify the Agencies’ analysis of this issue, stating that “efficiencies are most likely to make a difference in merger analysis when the likely adverse competitive effects, absent the efficiencies, are not great. Efficiencies almost never justify a merger to monopoly or near-monopoly.”⁴⁶

In sum, the efficiencies section of the Guidelines:

- Explains how efficiencies may affect the analysis of whether a proposed merger may likely lessen competition substantially in a relevant market. This would depend on the extent to which the efficiencies enhance the merged firm’s capacity to behave competitively and, in turn, result in lower prices, improved quality, enhanced service or new products.
- Defines which efficiencies are attributable to a proposed merger and which likely could be achieved in other ways without posing as great a cost to competition.
- Clarifies what parties will have to do to demonstrate claimed efficiencies.
- Sets forth how efficiencies are factored into the analysis of the competitive effects of a merger and indicates how delays in realizing the benefits of efficiencies will be treated.

Efficiencies are relevant in both a coordinated interaction context (e.g., where marginal cost reductions may make coordination less likely) and a unilateral effects context (e.g., where marginal cost reductions may reduce the merged firm’s incentive to elevate price). A merger, however, will still be condemned as anticompetitive under the Guidelines if the overall effect is to lessen competition in a relevant market.

⁴⁶ *Id.* at § 4.

The Agencies will consider only “merger-specific efficiencies,” *id est* only those “likely to be accomplished with the proposed merger and unlikely to be accomplished in the absence of either the proposed merger or another means having comparable anticompetitive effects.”⁴⁷ The Agencies will not insist on a less restrictive alternative to the merger if it is “merely theoretical.”⁴⁸ The Agencies will not consider efficiencies to be merger-specific if they could alternatively be achieved by divestiture and licensing instead of merger, thereby mitigating rather than increasing anticompetitive concerns.⁴⁹

The Guidelines note that the burden of proof with respect to efficiencies resides with the proponents of the merger.⁵⁰ This is consistent with recent judicial decisions.⁵¹ Furthermore, the Guidelines stress that because much of the information relating to efficiencies is “uniquely in the possession of the merging parties,”⁵² and because projected efficiencies are in any case difficult to verify and quantify, the burden is on the merging parties to substantiate with specific information, rather than vague and speculative arguments, “the likelihood and magnitude of each asserted efficiency, how and when each would be achieved (and any costs of doing so), how each would enhance the merged firm’s ability and incentive to compete, and why each would be merger-specific.”⁵³

While the Agencies’ reviews look to the effects of competition in each relevant market affected by the merger, the Agencies now also consider “efficiencies not strictly in the relevant market, but so inextricably linked with it that a partial divestiture or other remedy could not feasibly eliminate the anticompetitive effect in the relevant market without sacrificing the efficiencies in the other market(s).”⁵⁴

The Guidelines provide some examples of cognizable efficiencies, although they are now described in arguably more abstract terms than in the previous § 4. Previously, § 4 specified “economies of scale, better integration of production facilities, plant specialization, lower transportation costs, and similar efficiencies relating to specific manufacturing, servicing, or

⁴⁷ *Id.*

⁴⁸ *Id.*

⁴⁹ *Id.* at n.35.

⁵⁰ *Id.* at § 0.1 n.5.

⁵¹ *See, e.g.,* FTC v. Univ. Health, Inc., 938 F.2d 1206 (11th Cir. 1991).

⁵² Merger Guidelines, § 4.

⁵³ *Id.*

⁵⁴ *Id.* at § 4 n.36.

distribution operations of the merging firms,” in addition to claimed efficiencies from reductions in general selling, administrative and overhead expenses.⁵⁵ With a broader brush – and ostensibly without repudiating the more detailed but non-exhaustive list of before – the new § 4 cites as examples of cognizable efficiencies those resulting from shifting production among facilities that were formerly owned separately, which thereby reduces the marginal cost of production: these are considered more likely than many other types of efficiencies “to be susceptible to verification, merger-specific, and substantial, and are less likely to result from anticompetitive reductions in output.”⁵⁶ Efficiencies relating to procurement, management, or capital cost are cited as examples of efficiencies less likely to be merger-specific or substantial.⁵⁷

In a 1999 law review article, current FTC Chairman Timothy Muris, then a law professor at George Mason University School of Law, noted that the Merger Guidelines did not seem to sufficiently credit mergers which showed that they were likely to reduce costs.⁵⁸ The article examined the Guidelines’ presumption of illegality based on certain levels of concentration, and suggested that this presumption might sometimes bias the review process against efficiencies.⁵⁹ The article also suggested that the Guidelines perhaps did not encourage a full examination of the “broad range of efficiency that mergers can produce.”⁶⁰ The article suggested broadening the categories of efficiencies that would be deemed “cognizable”⁶¹ and that the government may wish to view capital-raising efficiencies and managerial economies in a different light.⁶²

Chairman Muris recently spoke about efficiencies in a FTC roundtable speech.⁶³ He stated that efficiencies can and should play an important role in merger analysis.⁶⁴ He also

⁵⁵ U.S. Department of Justice and Federal Trade Commission 1992 Horizontal Merger Guidelines (issued Apr. 2, 1992), *available at* 1992 WL 216553.

⁵⁶ Merger Guidelines (with 1997 revision), § 4.

⁵⁷ *Id.*

⁵⁸ Timothy J. Muris, *The Government and Merger Efficiencies: Still Hostile After All These Years*, 7 GEO. MASON L. REV. 729, 739 (Spring 1999).

⁵⁹ *Id.* at 737 - 40.

⁶⁰ *Id.* at 733.

⁶¹ *See* Merger Guidelines, § 4. The Guidelines define “cognizable efficiencies” as “merger-specific efficiencies that have been verified and do not arise from anticompetitive reductions in output or service.” *Id.*

⁶² Muris, *supra* note 58.

⁶³ Timothy J. Muris, Remarks at the FTC’s Roundtable on “Understanding Mergers: Strategy and Planning, Implementation, and Outcomes” (Dec. 9, 2002) (transcript available at <http://www.ftc.gov/speeches/muris/mergers021209.htm>).

acknowledged that while efficiencies are unlikely to outweigh the likely anticompetitive effects of a three-to-two or a two-to-one merger in a market with high entry barriers, under other circumstances efficiencies can help tip the balance in favor of agency approval, citing the Commission's approval of the merger between AmeriSource Health Corp. and Bergen Brunswig Corp., the third and fourth largest drug wholesalers in the country.⁶⁵

Chairman Muris seems to disagree with the view that structural considerations alone dictate the analysis,⁶⁶ explaining that neither the Guidelines nor FTC enforcement policy use that approach while also acknowledging that some courts seem to have taken such a position.⁶⁷

Chairman Muris made a final point that the Commission needs evidence to support prospective efficiencies, otherwise the Commission would not be able to properly weigh efficiencies in the balance and accurately assess a merger's competitive impact.⁶⁸

Not all agree with the Chairman, however, and this is an area which will most likely evolve over time.⁶⁹

Although the DOJ has not spoken as clearly as Chairman Muris on this subject, there is reason to believe that the Antitrust Division might similarly accord greater weight to efficiencies. Companies and their counsel should revisit this subject because efficiencies may play a more prominent role, although changes will probably occur mostly at the margins of pre-existing enforcement policy. Also, the Agencies will almost certainly continue to be unsympathetic to unsubstantiated, abstract, or sloppy efficiencies claims.

G. Failure and Exiting Assets

The failing-firm defense allows an otherwise objectionable transaction to be cleared regardless of its effects on competition.⁷⁰ It has stringent criteria because it is the only absolute

⁶⁴ *Id.*

⁶⁵ News Release, Federal Trade Commission, Federal Trade Commission Votes to Close Investigation of Proposed Merger of Amerisource Health Corporation and Bergen Brunswig Corporation (Aug. 24, 2001) (*available at* <http://www.ftc.gov/opa/2001/08/amerisourcebergen.htm>).

⁶⁶ An example of a structural consideration is a very high HHI.

⁶⁷ *See, e.g.,* FTC v. H.J. Heinz, Co., 116 F. Supp. 2d 190 (D.D.C. 2000), *rev'd*, 246 F.3d 708 (D.C. Cir. 2001).

⁶⁸ Muris remarks, *supra* note 63.

⁶⁹ *See, e.g.,* Thomas B. Leary, *Efficiencies and Antitrust: A Story of Ongoing Evolution*, ABA SECTION OF ANTITRUST LAW FALL 2002 FORUM (Nov. 8, 2002).

⁷⁰ Merger Guidelines, § 5.1.

defense U.S. merger law allows. While the failing-firm defense is rarely upheld and its use has been repeatedly unsuccessful in FTC administrative proceedings, it was recently the basis for the DOJ's approval of the acquisition of a failing newspaper by its rival.⁷¹

The Guidelines list four conditions precedent to successfully invoke the failing-firm defense. First, failure must be imminent. Second, there must be a showing that the firm would be unable to reorganize in bankruptcy. Third, the party invoking the defense must establish that no alternative purchasers exist. Fourth, the proponents of this defense must demonstrate that "absent the acquisition, the assets of the failing firm would exit the relevant markets."⁷²

With regard to the failing firm's obligation to seek reasonable alternative offers from less objectionable acquirers, a "reasonable" offer under the Guidelines is "[a]ny offer to purchase the failing firm for a price above the liquidation value of those assets – the highest valued use outside the relevant market or equivalent offer to purchase the stock of the failing firm – will be regarded as a reasonable alternative offer."⁷³

Consistent with the Guidelines, the FTC's report on the global competition hearings recommends that the defense not be expanded but urges firms that are "failing" or in distressed circumstances to ask the Agencies to consider their financial condition as part of the overall assessment of the competitive effects of the transaction.⁷⁴

II. RECENT MERGER ENFORCEMENT BY THE FEDERAL AGENCIES

The great majority of transactions reported under HSR present no competitive issues. The Guidelines explicitly recognize that most mergers are competitively neutral or procompetitive,⁷⁵ and the statistics confirm this. The Agencies continue to pursue enforcement in the merger area aggressively, but also flexibly.

After HSR review the Agencies may (1) clear a transaction as it is structured, (2) approve a transaction only upon the merging parties agreeing to specified conditions (e.g. divestiture of assets), or (3) seek to block a transaction in its entirety. The overwhelming majority of transactions submitted for HSR review are approved without condition. When the Agencies

⁷¹ This was the 1995 purchase of THE HOUSTON POST by THE HOUSTON CHRONICLE. See, e.g., David Segal, *111-Year Old Houston Post is Shut Down; Rising Cost of Newsprint Cited for Sale to Owner of Rival Chronicle*, THE WASH. POST, Apr. 19, 1995 at F4.

⁷² Merger Guidelines, § 5.1.

⁷³ *Id.* at § 5.1 n.39.

⁷⁴ See generally Special Report, Executive Summary and Principal Conclusions, FTC Staff Report, *Competition Policy in the New High-Tech, Global Marketplace*, 64 ANTITRUST L.J. 791 (Spring 1996).

⁷⁵ Merger Guidelines, § 0.1.

review a problematic transaction, they usually first seek to resolve the competitive issues by a consent decree rather than by challenging the transaction in its entirety.

After the FTC or DOJ conducts its detailed investigation of more problematic transactions, based in part on information it receives in response to its formal request for additional documents and information, it may seek to negotiate an agreement with the parties. Such agreements often call for partial divestiture of assets, the erection of “firewalls” to prevent the exchange of competitively sensitive information within an entity resulting from a vertical merger, and other related measures intended to prevent possible anticompetitive effects resulting from a merger. The FTC will issue a complaint at the same time as a proposed consent agreement if an agreement is reached. The public then has 60 days, sometimes longer, to comment on the transaction, after which the agreement may or may not be modified in response to such comment, and the Agency will issue a final consent order.

Similarly, the DOJ will usually issue a complaint at the same time as a proposed consent agreement. The Tunney Act gives the public 60 days to comment on the agreement, after which the agreement, in original or revised form, will be submitted to a federal district court judge for a fairness hearing, where the judge determines whether the agreement is in the interest of the public.⁷⁶ The court will enter the agreement as an order if it approves.

Alternatively, the Agencies may seek to block the transaction. In this scenario, the reviewing Agency usually first moves in federal court for a preliminary injunction. The DOJ is authorized to continue in federal court at this point and seek either a permanent injunction or modification of the transaction. With the FTC, if the motion is granted, the enforcement action continues before an administrative law judge. After a successful motion for a preliminary injunction, the FTC has 20 days within which to file a complaint with an administrative law judge. If the motion is denied, the FTC may still file a complaint but has more than 20 days. The FTC issues a complaint when it has “reason to believe” that the law has been or is being violated, and it appears to the Commission that a proceeding is in the public interest. The administrative law judge reviews the allegations in a formal hearing and renders a decision. The process may take six months to one year. This decision then goes back to the Commission for a vote;⁷⁷ its decision may then be appealed to the appropriate United States Court of Appeals.

Standards for preliminary injunctive relief. Section 13(b) of the FTC Act authorizes the Commission in a “proper case” to seek permanent injunctive relief against entities that have

⁷⁶ 15 U.S.C. § 16, § 5 of the Clayton Act.

⁷⁷ The Commission will not necessarily uphold an administrative law judge’s ruling against a transaction, even though the Commission itself authorized the filing of the complaint. For example, the Commission’s composition may have changed in the interim. Furthermore, the standards for filing a complaint and the standards for voting on an ALJ’s ruling are different.

violated or threaten to violate any of the laws under the FTC's jurisdiction.⁷⁸ In merger cases the FTC commonly uses §13(b) to seek a preliminary injunction in order to preserve the status quo pending an administrative hearing. The §13(b) standard for issuing a preliminary injunction is "[u]pon a proper showing that, weighing the equities and considering the Commission's ultimate likelihood of success, such action would be in the public interest."⁷⁹ With respect to the DOJ, courts have applied various standards to motions for preliminary injunctive relief, ranging from establishing a reasonable probability that it will ultimately prevail on the merits to a requirement that it only has to raise serious questions of law and fact, but not requiring proof of irreparable injury or substantial harm to the public, unlike the typical public interest standard.⁸⁰ Successful preliminary injunctions often terminate an acquisition effort, and so is an important strategic issue to remember.

As a practical matter, a court may – and the DOJ often agrees to – consolidate proceedings on a motion for preliminary injunctive relief with a trial on the merits of the DOJ's request for a permanent injunction.⁸¹ If so, the DOJ has the full burden of proving a Section 7 claim by a preponderance of evidence.⁸² These different burdens of proof can be important when either agency seeks to enjoin a merger.

The following discussion details certain notable merger analyses by the Agencies in 2003.

⁷⁸ 15 U.S.C. § 53(b) (2002).

⁷⁹ *Id.* Some circuits agree with the view that "it will ordinarily be enough that the plaintiff has raised serious legal questions going to the merits, so serious, substantial, difficult as to make them a fair ground of litigation and thus for more deliberative investigation." *Population Inst. v. McPherson*, 797 F.2d 1062, 1078 (D.C. Cir. 1986) (citing *Washington Metro. Area Transit Comm'n v. Holiday Tours, Inc.*, 559 F.2d 841, 844 (D.C. Cir. 1977)). *See also* *Safety-Kleen, Inc. (Pinewood) v. Wyche*, 274 F.3d 846, 859 (4th Cir. 2001) (stating that "[i]f the harm balance 'tips decidedly in favor of the plaintiff, a preliminary injunction will be granted if the plaintiff has raised questions going to the merits so serious, substantial, difficult and doubtful, as to make them fair ground for litigation and thus for more deliberate investigation.'" (citing *Rum Creek Coal Sales, Inc. v. Caperton*, 926 F.2d 353, 359 (4th Cir. 1991) (internal quotation marks and citation omitted))). In other words, the movant must, at the very least, present a substantial question.

⁸⁰ *See, e.g.,* *Wooten v. First Nat'l Bank of St. Paul, Minn.*, 490 F.2d 1275, 1276 (8th Cir. 1974) (citing *Brown v. Chote*, 411 U.S. 452 (1973), and *Telex Corp. v. Int'l Bus. Mach. Corp.*, 464 F.2d 1025 (8th Cir. 1972)).

⁸¹ From the DOJ's perspective, it may be unduly repetitive to prepare and present evidence and arguments for a preliminary injunction hearing and then, assuming the Division wins its motion, have to return to court shortly thereafter for a full trial on the merits.

⁸² *United States v. SunGard Data Sys., Inc.*, 172 F. Supp.2d 172 (D.D.C. 2001) (placing the full burden of proof on the government for a § 7 case because the DOJ agreed to consolidate its motion for preliminary injunctive relief with a trial on the merits of its demand for a permanent injunction).

A. Horizontal Mergers

1. Pfizer/Pharmacia

On April 14, 2003 the FTC announced that Pfizer, Inc. ("Pfizer") and Pharmacia Corporation ("Pharmacia") would divest pharmaceutical products in nine separate product markets to different third parties in order to settle FTC charges that the Pfizer/Pharmacia merger would likely have anticompetitive effects in those product markets and violate antitrust laws.⁸³ The products include extended release drugs for the treatment of overactive bladder; combination hormone replacement therapies; treatments for erectile dysfunction; drugs for canine arthritis; antibiotics for lactating cow mastitis; antibiotics for dry cow mastitis; over-the-counter hydrocortisone creams and ointments; over-the-counter motion sickness medications; and over-the-counter cough drops.⁸⁴

With worldwide revenues of over \$32 billion, Pfizer, a Delaware corporation based in New York, is the largest pharmaceutical company in the United States, the largest animal health pharmaceutical company in the world, and one of the world's largest providers of consumer health products.⁸⁵ Pharmacia, based in Peapack, New Jersey, is engaged in the research, development, manufacture, and sale of pharmaceutical products, animal health products, fine chemicals, and consumer health products. Pharmacia reported 2001 sales revenues of over \$13.8 billion, with \$11.9 billion realized from prescription pharmaceutical sales. Pfizer proposed to acquire Pharmacia in a deal valued at approximately \$60 billion.⁸⁶

The first product market examined by the FTC was for extended release drugs treating overactive bladder (OAB), which are used by over 2.4 million Americans. U.S. annual sales of extended release OAB products total approximately \$760 million.⁸⁷ According to the FTC, there were only two significant players in the U.S. market for extended release OAB products: Pharmacia and Johnson & Johnson. Pfizer was seeking approval from the Food and Drug Administration (FDA) to market its own extended release product. According to the FTC, Pfizer and another company called Yamanouchi Pharma America were the two best-positioned firms seeking to enter the market.⁸⁸

⁸³ News Release, Federal Trade Commission, Pfizer, Pharmacia Will Divest Assets to Settle FTC Charges (Apr. 14, 2003) (*available at* <http://www.ftc.gov/opa/2003/04/pfizer.htm>).

⁸⁴ *Id.*

⁸⁵ *Id.*

⁸⁶ *Id.*

⁸⁷ *Id.*

⁸⁸ *Id.*

The FTC alleged that the proposed acquisition would cause significant anticompetitive harm in the U.S. market for extended release OAB products by eliminating potential competition between Pfizer and Pharmacia. The FTC believed that Pfizer's and Yamanouchi's entry into the market would likely increase competition and reduce prices for extended release OAB products. Thus, the proposed consent agreement required that Pfizer divest its extended release OAB product to Novartis AG as well as certain other assets designed to ensure the divestiture's success.⁸⁹

The second product market analyzed was the one for combination hormone replacement therapies (HRT), which consists of both estrogen and progestin and are used by women to alleviate menopausal symptoms. Total domestic sales of combination HRT products in 2002 were approximately \$807 million. According to the FTC, there were three significant competitors in the combination HRT market: Wyeth, Pfizer, and Pharmacia. The proposed consent agreement required the parties to divest Pfizer's combination HRT product to Galen Holdings PLC. The agreement contained certain other provisions designed to ensure the divestiture's success.⁹⁰

The third product market evaluated was for erectile dysfunction (ED), which affects 30 million men in the United States and half of the male population between the ages of 40 and 70. Approximately 4 million men take prescription drugs to treat ED. The U.S. market for drugs to treat ED is currently valued at over \$1 billion and is expected to exceed \$1.5 billion by 2005 as the population ages and awareness of the condition increases.⁹¹ According to the FTC, Pfizer's popular product, Viagra, dominates the ED market with its domestic market share of over 95 percent. Pfizer also has a second-generation Viagra-like product in development. Pharmacia currently has two products in clinical development for ED.⁹²

The consent agreement therefore required Pharmacia to return all of its rights in one of its ED products to Natesth Pharmaceutical Company, Inc. and to divest all of its rights and interests for the field of sexual dysfunction in its other product to Neurocrine Biosciences, Inc. The agreement contained certain other provisions designed to ensure that the divestiture's success.⁹³

⁸⁹ *Id.*

⁹⁰ *Id.*

⁹¹ For example, former Senator Bob Dole (R-KS) has made several ED-related commercials and public service announcements.

⁹² News Release, Federal Trade Commission, Pfizer, Pharmacia Will Divest Assets to Settle FTC Charges, (Apr. 14, 2003) (*available at* <http://www.ftc.gov/opa/2003/04/pfizer.htm>).

⁹³ *Id.*

The fourth product market assessed was for canine arthritis. Approximately 1.8 million arthritic dogs are treated with prescription canine arthritis drugs. Domestic sales in 2001 for prescription canine arthritis drugs totaled approximately \$81 million. The U.S. market is expected to grow to over \$110 million by the end of 2003.⁹⁴ According to the FTC, the prescription canine arthritis drug market is highly concentrated. The FTC found that Pfizer's leading product in the U.S. market, Rimadyl, held a 70 percent market share in 2001. Wyeth and Novartis, through a license and supply agreement with Pharmacia, market their own products. Because of this agreement, the FTC believed that the combined Pfizer/Pharmacia company would have undue control over the supply of product Novartis needed as well as access to Novartis' sensitive confidential information. The FTC alleged that this would place Pfizer in a position to undermine the competitive position of one of only two competitors in the market for prescription drugs to treat canine arthritis.⁹⁵

The consent agreement therefore required Pharmacia to renegotiate its pre-existing license and supply agreement with Novartis so that Novartis can operate as an independent competitor rather than a business partner. The settlement eliminated Pfizer's control over Novartis' product; restricted the type of information Pfizer would be able to obtain; and allowed Novartis to compete with Pfizer in the development of a second generation canine arthritis product.⁹⁶

The fifth and sixth product markets considered were for drugs to treat bovine mastitis, an infection of the udder of the cow, which costs the U.S. dairy industry \$2 billion annually. There are two different types of contagious bovine mastitis: (1) lactating cow mastitis; and (2) dry cow mastitis.⁹⁷ In the United States, \$27 million worth of lactating cow mastitis antibiotic products and \$25.5 million worth of dry cow mastitis antibiotic products are sold annually.⁹⁸

According to the FTC, the U.S. markets for bovine mastitis treatments are highly concentrated. The FTC found only three significant competitors in the markets for lactating cow and dry cow mastitis antibiotic products: Pharmacia, Wyeth, and Pfizer. According to the FTC, Pfizer, post-acquisition, would account for 50 percent of the sales of lactating cow mastitis

⁹⁴ *Id.*

⁹⁵ *Id.*

⁹⁶ *Id.*

⁹⁷ *Id.* See also, e.g., *Miscellaneous Mastitis Causing Organisms*, MASTITIS MODULE FACT SHEET, New York State Cattle Health Assurance Program, available at <http://nyschap.vet.cornell.edu/module/mastitis/section1/miscellaneous%20mastitis%20fact%20sheet.pdf>.

⁹⁸ News Release, Federal Trade Commission, Pfizer, Pharmacia Will Divest Assets to Settle FTC Charges, (Apr. 14, 2003) (available at <http://www.ftc.gov/opa/2003/04/pfizer.htm>).

products and 55 percent of the sales of dry cow mastitis products, leaving only one firm, Wyeth, as a significant competitor. The FTC alleged that this would likely to lead to higher prices for drugs used to treat bovine mastitis. Thus, the consent agreement required Pfizer to divest all of its U.S. rights to its bovine mastitis antibiotic products to Schering-Plough Corporation.⁹⁹

The seventh product market reviewed was for over-the-counter (OTC) hydrocortisone topical creams and ointments used to treat skin conditions, where annual sales approximated \$160 million. The FTC alleged that there were only two branded competitors in the market, Pfizer and Pharmacia. Although there are private label hydrocortisone creams that account for a significant market share, the FTC believed that those products had limited competitive significance and virtually no impact on the pricing of Pfizer's and Pharmacia's products. The FTC calculated that, post-acquisition, Pfizer would account for 55 percent of the OTC sales of hydrocortisone creams and ointments and would be left with no significant branded competitor in this market. Thus, the consent agreement required Pharmacia to divest its Cortaid, an OTC hydrocortisone cream, business to Johnson & Johnson.¹⁰⁰

The eighth product market analyzed was for OTC motion sickness medications, of which U.S. annual sales totaled approximately \$45 million. The FTC found that Pfizer, with its Bonine product, and Pharmacia, with its Dramamine product, were the two leading suppliers in this market, with a combined market share of 77 percent. The third leading brand name product, Marezine, had less than 5 percent of the market. The remainder of the market was accounted for by private label products that unlikely constrain the pricing of the branded products. Thus, the proposed consent agreement required Pfizer to divest its U.S. and Puerto Rican Bonine assets to Insight Pharmaceuticals Corporation.¹⁰¹

The ninth product market evaluated was for cough drops, of which U.S. annual sales were about \$240 million. The FTC found that Pfizer, with its Halls brand and Pharmacia, with its Ludens brand, were the only two significant competitors. Thus, the consent agreement required Pfizer to divest its Halls cough drop business to Cadbury Schweppes.¹⁰²

The settlement required all divestitures to occur no later than ten days after the Pharmacia acquisition is consummated. If the Commission determined that the specified buyers were not acceptable purchasers, the assets would have been divested to a Commission-approved buyer no later than six months from the date the order became final.¹⁰³

⁹⁹ *Id.*

¹⁰⁰ *Id.*

¹⁰¹ *Id.*

¹⁰² *Id.*

¹⁰³ *Id.*

The Commission voted 5 – 0 to accept the proposed settlement, and the agreement is subject to public comment until May 14, 2003, after which the Commission will decide whether to make it final.¹⁰⁴

2. Univision/Hispanic Broadcasting Corporation

On June 11, 2002 Univision Communications Inc. (“Univision”) proposed to acquire Hispanic Broadcasting Corporation (“HBC”) pursuant to an Agreement and Plan of Reorganization. Univision and HBC are two of the nation’s largest Spanish-language media companies.

On March 26, 2003 the DOJ filed suit in the U.S. District Court for the District of Columbia (Civil Action No. 1:03CV00758, RMC) to block this proposed transaction while simultaneously filing a proposed consent decree that would resolve the suit and the DOJ’s competitive concerns if approved by the Court.¹⁰⁵ The decree required Univision to sell a significant portion of its partial ownership interest in Entravision Communications Corporation (“Entravision”) and agree to other restrictions in order to proceed with its \$3 billion acquisition of HBC. The DOJ believed that, without these conditions, Univision’s acquisition of HBC would lessen competition in the sale of advertising time on many Spanish-language radio stations because HBC is Entravision’s principal competitor in Spanish-language radio in the following “Metro Survey Areas”: Dallas, Texas; El Paso, Texas; Las Vegas, Nevada; McAllen-Brownsville-Harlingen, Texas; Phoenix, Arizona; and San Jose, California.¹⁰⁶ The DOJ claimed that the combined company’s 30 percent equity stake and governance rights in Entravision would substantially reduce competition between Univision/HBC and Entravision, resulting in higher prices and reduced levels of service with respect to advertising time.¹⁰⁷

The proposed consent decree requires, *inter alia*, (1) Univision to divest its Entravision equity so that it holds no more than 15 percent of Entravision shares within three years and no more than 10 percent within six years, (2) Univision to exchange its Entravision stock for a non-voting equity interest with limited rights, and (3) Univision to relinquish its right to two seats on Entravision’s Board of Directors and its right to vote its shares or veto certain Entravision

¹⁰⁴ *Id.*

¹⁰⁵ Press Release, U.S. Department of Justice, Justice Department Requires Univision to Make Divestitures to Complete Acquisition of Hispanic Broadcasting Corporation (Mar. 26, 2003) (*available at* http://www.usdoj.gov/atr/public/press_releases/2003/200871.htm).

¹⁰⁶ A Metro Survey Area (MSA) is a geographical unit for which Arbitron, a company that surveys radio listeners, furnishes radio stations, advertisers, and advertising agencies in a particular area with data to aid in evaluating radio audience size composition. several geographic areas.

¹⁰⁷ Press Release, U.S. Department of Justice, Justice Department Requires Univision to Make Divestitures to Complete Acquisition of Hispanic Broadcasting Corporation (Mar. 26, 2003) (*available at* http://www.usdoj.gov/atr/public/press_releases/2003/200871.htm).

business decisions. Univision also may not improperly influence Entravision's radio business' conduct.¹⁰⁸

3. Nestlé/Dreyer's¹⁰⁹

Alleging a "superpremium" ice cream market, on March 4, 2003 the Commission voted 5 – 0 to authorize its staff to seek a preliminary injunction blocking the \$2.8 billion merger of Nestlé Holdings, Inc. and Dreyer's Grand Ice Cream, Inc., pending an administrative trial on the grounds that the transaction as originally structured would violate § 7 of the Clayton Act.¹¹⁰

In June 2002, Nestlé and Dreyer's proposed to combine Nestlé's Häagen-Dazs with Dreyer's Dreamery, Godiva, and Starbucks ice creams. According to the FTC, Nestlé and Dreyer's, along with Unilever, the marketer of Ben & Jerry's brand ice cream, account for about 98 percent of the relevant market of superpremium ice cream sales. The FTC stated that the purchase of Dreyer's would give Nestlé, alone, about 60 percent of that market.¹¹¹

Nestlé Holdings, based in Norwalk, Connecticut, is a subsidiary of Nestlé S.A., the world's largest food company. Nestlé's ice cream product sales in 2001 totaled approximately \$800 million. Dreyer's Grand Ice Cream, Inc., based in Oakland, California, sells products under the Dreyer's brand in thirteen western states and Texas, and under the Edy's brand name throughout the remaining regions of the United States. Dreyer's total 2001 sales were approximately \$1.4 billion.¹¹²

The FTC claimed that Dreyer's presence directly, persistently, and procompetitively impacted pricing, marketing and product introductions, which caused Nestlé to increase promotions and lower prices. The FTC believed that eliminating Dreyer's would likely lead to anticompetitive effects in the superpremium ice cream market, including less product variety and higher prices, and that entry into the market would not be likely or sufficient to outweigh the anticompetitive harm.¹¹³

¹⁰⁸ *Id.*

¹⁰⁹ Wags have taken to calling this the "ice cream merger."

¹¹⁰ News Release, Federal Trade Commission, FTC to Challenge Nestlé, Dreyer's Merger (Mar. 4, 2003) (*available at* <http://www.ftc.gov/opa/2003/03/dreyers.htm>).

¹¹¹ *Id.*

¹¹² *Id.*

¹¹³ *Id.*

4. Quest Diagnostics/Unilab

Following a public comment period, on April 3, 2003 the Commission approved, in a 5 – 0 vote, the issuance of a final consent order in the matter concerning the merger of Quest Diagnostics, Inc. (“Quest”) and Unilab Corporation (“Unilab”), the two leading lab testing firms in Northern California. On February 21, 2003 the FTC had proposed a consent order that would conditionally allow Quest’s \$827 million acquisition of Unilab, provided that the companies divest certain assets to Laboratory Corporation of America (“LabCorp”). The FTC was concerned that the original proposal would likely be anticompetitive¹¹⁴ and lead to higher prices for clinical laboratory services in Northern California because the combined firm’s market share in Northern California would have exceeded 70 percent.¹¹⁵ The threat of price increases would have been greatest to independent physician associations (IPAs) and other physicians groups that depend on the unique rivalry between Quest and Unilab to minimize healthcare costs.

The consent order required Quest and Unilab to divest the following to LabCorp: 46 patient service centers (PSCs); five stat (rapid response) laboratories; all of Quest’s and one of Unilab’s Northern California contracts with physicians groups; and all related assets necessary for the provision of clinical lab testing services to such groups, including customer lists and information. The FTC believed that this would allow LabCorp to replace competition that would be lost as a result of the proposed acquisition.¹¹⁶

Quest, headquartered in Teterboro, New Jersey, is the largest supplier of clinical lab testing services in the United States and the second-largest provider in California, with 2002 revenues of approximately \$4.1 billion. It has a nationwide network of approximately 1,350 patient service centers (PSCs), about 30 principal labs in metropolitan areas throughout the United States, and about 100 smaller stat laboratories. In California, Quest has three full-service testing laboratories, eight stat labs, and about 126 PSCs. One of Quest’s full-service laboratories, five of its stat laboratories and about 76 of its PSCs are located in Northern California.¹¹⁷

Unilab, based in Tarzana, California, is the largest supplier of lab testing services in California, with 2001 revenues of approximately \$390 million. Unilab has three full-service

¹¹⁴ By violating § 7 of the Clayton Act, 15 U.S.C. § 18, and § 5 of the FTC Act, 15 U.S.C. § 45.

¹¹⁵ News Release, Federal Trade Commission, FTC to Require Divestiture as Condition of Clearing Quest Diagnostics, Inc.’s Acquisition of Unilab Corporation (Feb. 21, 2003) (*available at* <http://www.ftc.gov/opa/2003/02/quest.htm>).

¹¹⁶ *In re Quest Diagnostics, Inc. and Unilab Corp.*, Docket No. C-4074, Decision and Order (Apr. 3, 2003), *available at* <http://www.ftc.gov/os/2003/04/questdo.pdf>.

¹¹⁷ News Release, Federal Trade Commission, FTC to Require Divestiture as Condition of Clearing Quest Diagnostics, Inc.’s Acquisition of Unilab Corporation (Feb. 21, 2003) (*available at* <http://www.ftc.gov/opa/2003/02/quest.htm>).

laboratories in San Jose, Sacramento, and Los Angeles, as well as about 39 stat laboratories and about 386 PSCs. In Northern California, Unilab operates two full-service laboratories, 23 stat laboratories, and about 230 PSCs.¹¹⁸

According to the FTC, IPAs and other physicians' groups require lab testing suppliers that have the infrastructure of PSCs, stat labs, and full-service testing labs necessary to serve all of their physician members.¹¹⁹ A lab testing supplier that already has infrastructure in the area served by a particular physicians' group will likely be able to service that group at a lower cost than a new entrant to the area could charge.¹²⁰

The FTC believed that the sale of clinical laboratory testing services to physicians groups was the relevant product market in which to analyze the competitive effects of the acquisition in Northern California, the relevant geographic region.¹²¹

The FTC approved LabCorp as a well-positioned acquirer of the divested assets for several reasons. First, LabCorp offers more than 4,000 clinical tests, as well as other services that physicians groups require, such as patient encounter and result data reporting information technology. Second, LabCorp had a limited presence in Northern California, primarily providing clinical reference testing to hospitals and esoteric HIV-related testing. Third, LabCorp had a great deal of experience meeting the requirements of physicians' groups in Southern California, especially considering California's managed care environment. Finally, LabCorp has the financial resources to buy the assets to be divested and to operate them in a competitive manner.¹²²

The consent order required Quest to consummate the assets sale to LabCorp within ten days of the merger, with the transfer to be completed within six months. If Quest did not do so, the Commission had the authority to appoint a trustee to divest either the company's outpatient clinical laboratory or entire clinical laboratory testing businesses in Northern California. If Quest transferred some of the assets to LabCorp, but LabCorp abandoned its effort to complete the transfer of the rest of the assets, Quest may be required to rescind the transaction and order Quest to divest its Northern California outpatient clinical laboratory testing business to a Commission-approved buyer within six months. If Quest does not do so, the FTC may appoint

¹¹⁸ *Id.*

¹¹⁹ *Id.*

¹²⁰ *Id.*

¹²¹ *Id.*

¹²² *Id.*

a trustee to divest either Quest's Northern California outpatient or entire clinical laboratory testing business.¹²³

The consent order also required Quest to do the following: (1) maintain the viability, marketability, and competitiveness of its clinical laboratory testing business assets in Northern California, pending their transfer to LabCorp; (2) provide to LabCorp necessary transitional services until the assets are completely divested and transferred; (3) not interfere with the employment of any workers relating to the divested assets; (4) provide incentives for certain employees to continue in their positions until the divestiture and to accept employment with LabCorp; (5) not solicit, for one year after asset divestiture, any of Quest's or Unilab's employees that accept employment offers from LabCorp; and (6) maintain the confidentiality of certain information related to the divested assets.¹²⁴

5. Dainippon/Bayer

On March 13, 2003 the FTC accepted a final consent order settling competitive concerns raised by a deal between Bayer Corporation ("Bayer") and Dainippon Ink and Chemicals, Incorporated ("Dainippon").¹²⁵ The consent order allowed Dainippon, via its U.S. subsidiary Sun Chemical Corp. ("Sun Chemical"), to acquire Bayer's high-performance pigment business, but the consent order also required Dainippon to divest Sun Chemical's perylene business to Ciba Specialty Chemicals, Inc. and Ciba Specialty Chemicals Corp. ("Ciba") or to another FTC-approved buyer.¹²⁶ Ciba is a diversified specialty chemicals company.¹²⁷ Perylenes are organic pigments used to impart unique shades of red to a number of products, including coatings, plastics and fibers.¹²⁸

The consent order allowed Ciba to obtain all necessary assets in order to replace the competition by Sun Chemical in the perylene market. These include the following: all of Sun Chemical's current perylene products; all perylene research and development; manufacturing technology; scientific know-how; technical assistance and expertise; customer lists; raw

¹²³ *Id.*

¹²⁴ *Id.* See also *In re* Quest Diagnostics, Inc. and Unilab Corp., Docket No. C-4074, Decision and Order (Apr. 3, 2003), available at <http://www.ftc.gov/os/2003/04/questdo.pdf>.

¹²⁵ *In re* Dainippon Ink & Chemicals, Inc., FTC File No. 021-0100, Decision and Order, Docket No. C-4073 (Mar. 13, 2003), available at <http://www.ftc.gov/os/2003/03/dainippondo.pdf>.

¹²⁶ See generally *In re* Dainippon Ink & Chemicals, Inc., FTC File No. 021-0100 (Jan. 31, 2003).

¹²⁷ Ciba Specialty Chemicals, Inc. homepage, at <http://www.cibasc.com>.

¹²⁸ News Release, Resolving Anticompetitive Concerns, FTC Clears Dainippon's Acquisition of Bayer Corp.'s High-Performance Organic Pigment Business (Jan. 31, 2003), available at <http://www.ftc.gov/opa/2003/01/dainippon.htm>.

materials; intermediate and finished product inventory; and perylene product names, colors, codes, and trade dress, including all associated identifying colors and trademarks.¹²⁹

The consent order also gave Ciba the opportunity to hire one or more of Sun Chemical's employees who have key responsibilities in the perylene business. An interim monitor will be appointed by the FTC to supervise the assets transfer and to ensure that Sun Chemical provides the required technical assistance to Ciba for one year after divestiture.¹³⁰

Finally, the consent order provided that if Sun Chemical's divestiture to Ciba did not occur, other remedies existed, such as requiring Dainippon to divest the assets to a FTC-approved buyer within 90 days. If not, the FTC was empowered to appoint a trustee to divest the assets in a manner consistent with the order.¹³¹

6. Baxter/Wyeth

On February 3, 2003 the FTC accepted a consent agreement permitting Baxter International, Inc.'s ("Baxter") \$316 million acquisition of Wyeth Corporation's ("Wyeth") generic injectable drug business.¹³² The relevant markets included certain general anesthetics, neuromuscular blocking agents, antiemetics, and new injectable iron replacement therapies.

The consent agreement required the companies to do the following: (1) divest all of Wyeth's assets relating to the general anesthetic Propofol to Faulding Pharmaceutical Co. ("Faulding") or another Commission-approved acquirer; (2) terminate all of Baxter's rights and interests in GensiaSicor's neuromuscular blocking agents and divest related assets to GensiaSicor; and (3) terminate Baxter's co-marketing agreement with Watson Pharmaceuticals, Inc. regarding Watson's new injectable iron replacement therapy ("NIIRT") by March 14, 2004.¹³³

The general anesthetics product market includes drugs such as Propofol, a general anesthetic commonly used for the induction and maintenance of anesthesia during surgical procedures and also as a sedative for patients who are mechanically ventilated. Propofol is the

¹²⁹ *In re Dainippon Ink & Chemicals, Inc.*, FTC File No. 021-0100, Decision and Order, Docket No. C-4073 (Mar. 13, 2003), available at <http://www.ftc.gov/os/2003/03/dainippondo.pdf>.

¹³⁰ *Id.*

¹³¹ *Id.*

¹³² *In re Baxter Int'l, Inc. and Wyeth*, FTC File No. 021-0171, Decision and Order, Docket No. C-4068 (February 3, 2003), available at <http://www.ftc.gov/opa/2003/02/baxterwyethdo.htm>.

¹³³ *Id.*

preferred anesthetic agent for out-patient surgery because of its short duration and superior safety profile. Annual U.S. sales of Propofol totaled between \$375 and \$400 million.¹³⁴

The consent agreement required Baxter/Wyeth to divest Wyeth's Propofol assets to Faulding no later than ten business days after the acquisition. Baxter/Wyeth also had to (1) provide transitional services to the Faulding relating to regulatory approvals and manufacturing, and in responding to, and defending against, any lawsuit, investigation or proceeding relating to Propofol; (2) provide incentives to certain employees to continue in their positions until the divestiture is accomplished; (3) provide Faulding an opportunity to enter into employment contracts with individuals who have experience relating to Wyeth's Propofol product for a period of six months from the assets divestiture date; (4) provide incentives to these individuals to accept employment with Faulding; (5) refrain from hiring any Faulding employees who have responsibility related to Propofol for one year following the divestiture date; and (6) take steps to maintain the confidentiality of Propofol-related confidential information.¹³⁵

The second and third product markets were the various antiemetics and neuromuscular agents, which have domestic sales in the tens of millions each. The consent agreement, in addition to terminating Baxter's rights and interests in GensiaSicor's products, required that assets related to GensiaSicor's products be divested no less than five business days after the acquisition.¹³⁶

The fourth product market was NIIRTs, which includes both injectable iron gluconate and iron sucrose and are used to treat iron deficiency in patients undergoing hemodialysis.¹³⁷ Annual U.S. sales of NIIRTs total approximately \$225 million.¹³⁸ Watson Pharmaceuticals has a co-promotional agreement with Baxter. The consent agreement required Baxter to terminate its co-marketing agreement with Watson within weeks of Watson's product's New Chemical

¹³⁴ Analysis of Agreement Containing Consent Orders to Aid Public Comment, Federal Trade Commission (Dec. 20, 2002), *available at* http://www.ftc.gov/os/2002/12/baxter_wyethanalysis.htm.

¹³⁵ *In re Baxter Int'l, Inc. and Wyeth*, FTC File No. 021-0171, Decision and Order, Docket No. C-4068 (February 3, 2003), *available at* <http://www.ftc.gov/opa/2003/02/baxterwyethdo.htm>.

¹³⁶ *Id.*

¹³⁷ Analysis of Agreement Containing Consent Orders to Aid Public Comment, Federal Trade Commission (Dec. 20, 2002), *available at* http://www.ftc.gov/os/2002/12/baxter_wyethanalysis.htm.

¹³⁸ *Id.*

Entity exclusivity.¹³⁹ The consent agreement permitted Baxter to continue developing and ultimately launch the iron gluconate product which it will acquire from Wyeth.¹⁴⁰

7. Wal-Mart Stores, Inc. v. Rodriguez¹⁴¹

On February 28, 2003, Wal-Mart and the Commonwealth of Puerto Rico settled their dispute arising from Wal-Mart's purchase of Supermercados Amigo, Inc. ("Amigo") and thirty-two of Amigo's stores for \$225 million.¹⁴² In November of 2002 the FTC approved the deal on the condition that Wal-Mart sell four of thirty-six Amigo stores which were in direct competition with Wal-Mart outlets.¹⁴³ This was the first time that the FTC determined that the traditional "supermarket" product market definition did not apply and included club stores in the relevant Puerto Rico markets, which may allow a greater number of supermarket mergers in the future.

Two weeks after the FTC preliminary accepted the consent agreement and one day after the transaction closed, the Commonwealth of Puerto Rico filed suit in state court.¹⁴⁴ This case is one of the somewhat uncommon instances where federal and state enforcers are at odds.¹⁴⁵

The District Court in Puerto Rico granted Wal-Mart's motion for an injunction enjoining the Commonwealth of Puerto Rico from attempting to block Wal-Mart's acquisition of the Supermercados Amigo, Inc. supermarket chain. The District Court found that the Commonwealth's antitrust complaint in Commonwealth Court violated Wal-Mart's Commerce Clause and Equal Protection rights.¹⁴⁶

¹³⁹ *In re Baxter Int'l, Inc. and Wyeth*, FTC File No. 021-0171, Decision and Order, Docket No. C-4068 (February 3, 2003), available at <http://www.ftc.gov/opa/2003/02/baxterwyethdo.htm>.

¹⁴⁰ *Id.*

¹⁴¹ 238 F. Supp. 2d 395 (Dist. P.R. 2002), *remanded with instructions to vacate and dismiss* by 322 F.3d 747 (1st Cir. 2003).

¹⁴² *Latin America: Puerto Rico, Wal-Mart in Deal*, ORLANDO SENTINEL, Mar. 5, 2003 at C3.

¹⁴³ Mark Hamstra, *FTC Sets Precedent With Ruling, Allows Amigo Acquisition in P.R.; Wal-Mart's Acquisition of Supermercados Amigos*, SUPERMARKET NEWS, Dec. 2, 2002 at 4.

¹⁴⁴ Wal-Mart Stores, Inc., Docket No. C-4066, available at <http://www.ftc.gov/os/2002/11/walmartamigoagreement.pdf>.

¹⁴⁵ Another example is *California v. Am. Stores, Inc.*, 495 U.S. 271 (1990).

¹⁴⁶ 238 F. Supp. 2d at 414 - 420.

During the appeal of the decision to the 1st Circuit, the matter settled on February 28, 2003. The 1st Circuit subsequently remanded with instructions to vacate and dismiss with prejudice.¹⁴⁷

Under the settlement, Wal-Mart agreed to divest two supermarkets in addition to the four it had already divested under an FTC consent agreement. In addition, Wal-Mart agreed to maintain the current employment levels at the acquired stores and its current levels of local agricultural purchases for ten years. The company also certified that the four stores already divested had been sold for a fair price in an arm's-length transaction.

The settlement eases a controversy created in the District of Puerto Rico when Judge Perez-Gimenez enjoined the Secretary of Justice of the Commonwealth of Puerto Rico from pursuing a state court action or taking any other step to interfere with the acquisition. The court labeled Puerto Rico's antitrust claims "pretextual," "bogus," and "fabricated," and found that the state suit was brought to retaliate against Wal-Mart because Wal-Mart refused to buckle under politically motivated demands that Wal-Mart retain Amigo's existing labor force and guarantee minimum purchase levels of local agricultural products.¹⁴⁸ The court held that the Secretary's action violated the Commerce Clause and also denied Wal-Mart and Amigo equal protection.¹⁴⁹

The district court's order is important because by blocking a state antitrust suit on Commerce Clause grounds, the court opened the way for similar claims in future antitrust cases which would undercut the states' bargaining leverage in settlement negotiations. The order also threatened the states' role in merger enforcement because it suggested that Puerto Rico should have deferred to the FTC's analysis and remedy.

Antitrust federalism issues will likely continue in the foreseeable future, if only because state antitrust laws are not necessarily preempted by federal law and state attorneys general sometimes have statutory authority to seek damages or injunctive relief via *parens patriae*, among other things.¹⁵⁰

While many people are aware of the state attorneys general aggressively pursuing their interests in the Microsoft case, state action cases such as the Wal-Mart case and health care cases such as *FTC v. Butterworth Health Corp.*, 121 F.3d 708 (6th Cir. 1997) will likely see more activity from the state attorneys general that might conflict with the federal enforcers.

¹⁴⁷ 322 F.3d at 749.

¹⁴⁸ 238 F. Supp. 2d at 410, *passim*.

¹⁴⁹ *Id.* at 414 – 420.

¹⁵⁰ See, e.g., *Am. Stores, Inc.*, 495 U.S. at 271, and 15 U.S.C. § 15(c) (2003).

B. VERTICAL MERGERS

Although 2003 did not produce any particularly remarkable vertical merger cases, it is instructive to compare the results of two 2002 vertical merger cases, Cytac/Digene and Synopsys/ Avant!, where different facts led to different results.¹⁵¹

Cytac/Digene involved the merger of two complementary cervical cancer screening tests, where the companies may have had incentive to act anticompetitively. The FTC was concerned that the combined firm could use its market power in one market, liquid-based Pap tests, to impede competition in another market, DNA-based HPV tests.¹⁵² The FTC voted to block the merger¹⁵³ and the parties abandoned the merger before the FTC filed to enjoin the transaction in federal district court.

Synopsys/ Avant! involved two manufacturers of tools used in the electronic design industry to design integrated circuits for a number of common electronic devices. Synopsys had a dominant market share in “front-end” logic synthesis tools and Avant! had a significant market share in “back-end” place and route tools.¹⁵⁴ Each portion is essential to an integrated circuit. The FTC noted that the combined company had a strong incentive and ability to create an improved, more integrated product, which would benefit consumers.¹⁵⁵ The FTC also noted, however, that it was also possible for Synopsys to have an incentive to *limit* interoperability with Avant!’s competitors’ products.¹⁵⁶ Such behavior, however, would potentially antagonize

¹⁵¹ Vertical mergers involve two companies that have a customer-supplier relationship. They typically attract less enforcement attention than horizontal mergers because of the frequent presence of significant efficiencies and a less direct impact on competition.

¹⁵² The FTC was also concerned that this could possibly thwart future entrants by making it more difficult for them to secure FDA approvals.

¹⁵³ News Release, Federal Trade Commission, Federal Trade Commission Seeks to Block Cytac Corp.’s Acquisition of Digene Corp. (Jun. 24, 2002) (*available at* http://www.ftc.gov/opa/2002/06/cytac_digene.htm).

¹⁵⁴ Luz Park, *EDA Provider Diversifies with TFT – LCD Software*, ASIA BIZ TECH, Feb. 2002, *available at* http://neasia.nikkeibp.com/nea/200202/intvw_167421.html.

¹⁵⁵ *See, e.g.*, Statement of Commissioner Sheila F. Anthony, Synopsys, Inc./ Avant! Corp., File No. 021 – 0049 (Jul. 26, 2002), *available at* <http://www.ftc.gov/os/2002/07/advantanthonystmnt.htm>

¹⁵⁶ *See, e.g.*, Statement of Commissioner Timothy B. Leary, Synopsys, Inc./ Avant! Corp., File No. 021 – 0049 (Jul. 26, 2002), *available at* <http://www.ftc.gov/os/2002/07/avantlearystmnt.htm>.

customers and make the behavior neither advantageous nor profitable. Thus, the FTC found it questionable as to whether Synopsys/Avant! would limit the interoperability of its products.¹⁵⁷

The circumstances of the Cytyc/Digene transaction did not provide for this rationale, and thus it is an important factual, if nuanced, difference between the Synopsys/Avant! and Cytyc/Digene mergers.

On October 24, 2002, Joseph Simons, Director of the FTC's Bureau of Competition, spoke about the FTC's enforcement activities, including the Cytyc/Digene and Synopsys/Avant! mergers.¹⁵⁸

In his remarks, Director Simons pointed out that the Commission considered all the relevant facts during its investigations before taking action.¹⁵⁹ Comparing the reviews of Cytyc/Digene and Synopsys/Avant!, Director Simons noted that while "there were plenty of theories of competitive harm, at bottom, there just was not enough evidence that Synopsys would have either the incentive or the ability to foreclose competitive products sufficiently to harm consumers."¹⁶⁰ Director Simons also said that the Commission "took a hard look at all the facts, put its theoretical concerns aside, and voted unanimously to allow the [Synopsys/Avant!]merger."¹⁶¹ In reviewing both Cytyc/Digene and Synopsys/Avant!, Director Simons said, "the outcome in each case was dictated by the facts, not by any predisposition [of the Commission] towards or against vertical mergers."¹⁶²

These examples and Director Simons' remarks show that the FTC continues to examine the factual circumstances of proposed mergers very carefully.

CONCLUSION

The 1992 Merger Guidelines set forth the process of merger analysis by which the U.S. antitrust enforcement agencies identify mergers that are likely to create or facilitate the exercise of market power, possibly violating federal antitrust laws such as Section 7 of the Clayton Act.

¹⁵⁷ See, e.g., Statement of Commissioner Mozelle W. Thompson, Synopsys, Inc./Avant! Corp., File No. 021 - 0049 (Jul. 26, 2002), available at <http://www.ftc.gov/os/2002/07/avantthompsonstmt.htm>.

¹⁵⁸ Joseph J. Simons, Remarks at the Tenth Annual Golden State Antitrust and Unfair Competition Law Institute, ANTITRUST AND UNFAIR COMPETITION LAW SECTION OF THE STATE BAR OF CALIF. (Oct. 24, 2002) (transcript available at <http://www.ftc.gov/speeches/other/021024mergeenforcement.htm>).

¹⁵⁹ *Id.*

¹⁶⁰ *Id.* (emphasis in original)

¹⁶¹ *Id.*

¹⁶² *Id.*

Efficiencies is a likely area of much debate and evolution, even within the Agencies internally. Just a few months into 2003 we see that domestic merger activity continues accompanied by antitrust enforcement activity. Therefore, in order to analyze a potential transaction, it is important to have a thorough understanding of the Merger Guidelines and their application along with a familiarity of the Agencies' actual enforcement record. Understanding a state's antitrust laws, the politics and policies driving a state's attorney general, and the constitutional issues which arise from a federal/state conflict are also important.