

Antitrust Advisory

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Eleventh Circuit Upholds FTC's Merger Ruling and Divestiture Order

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In a recent ruling, reinforcing the Federal Trade Commission's (FTC) aggressive merger policy, the United States Court of Appeals for the Eleventh Circuit upheld a FTC decision condemning a merger of two could-be rivals, and also rejected challenges to the FTC's remedial order requiring complete divestiture. *Polypore International, Inc. v. Federal Trade Commission*, No. 11-10375, 2012 U.S. App. LEXIS 14195 (11th Cir. July 11, 2012). The decision is also noteworthy in its (and the FTC's) treatment of the potential competition issue, the use of the anticompetitive presumption in such circumstances, and the questions of market definition raised in the case.

In 2008, Polypore International Inc. (Polypore), a manufacturer of components used in batteries and medical devices, acquired fellow battery separator company Microporous Products, LP (Microporous) for \$76 million. The FTC filed an administrative complaint in September 2008 challenging the transaction. In particular, the Commission alleged that the deal substantially reduced competition in four distinct markets for battery separators: car batteries, golf cart batteries, motive batteries used in industrial equipment, and batteries used in uninterruptible power supplies. Battery separators are membranes installed between the positive and negative plates in flooded lead-acid batteries to prevent short circuits and to regulate the flow of electrical current between the plates.

Some important factors underlying the discussion below were that: (1) although Microporous had been investigating entry into the automotive batteries market for several years, it did not actually sell the product; (2) Microporous operated one Tennessee plant and had constructed one in Austria, which was not yet operational and was intended to serve European customers; (3) Microporous had also purchased equipment for another production line ("line in boxes"), which constituted some of the acquired assets; (4) for deep-cycle batteries, Microporous had the industry standard product, with approximately 90% of the market, despite higher prices; and (5) in the motive battery market, Polypore's subsidiary had the 90% market share.

After a four-week hearing, FTC Chief Administrative Law Judge D. Michael Chappell held that the acquisition was reasonably likely to substantially lessen competition in four relevant markets. He ordered divestiture of all acquired assets, including the plant in Austria. The Commission unanimously affirmed the decision for three of the relevant markets, including in its divestiture order the Austrian plant.

The heart of Polypore's appeal was that the FTC erred by treating the transaction as between actual competitors in the automotive battery markets rather than potential competitors, and then improperly relied upon the presumption of liability in horizontal mergers established by the Supreme Court in *United States v. Philadelphia National Bank*, 374 U.S. 321 (1963). Polypore argued that the potential competition doctrine applied because Microporous had not entered the automotive battery market by the time of the acquisition.

The Supreme Court has not issued a merger opinion since 1974, so it is no surprise that the Eleventh Circuit had to reach back 40 and 50 years to find relevant Supreme Court precedent. The court found *United States v. El Paso Natural Gas Co.*, 376 U.S. 651 (1964) instructive on the actual versus potential competition point. Like the natural gas situation at issue in *El Paso*, Microporous was already making similar separators. It would need only to retool a production line, and had purchased a new one. It had begun discussions with several companies, had

produced a satisfactory sample product with one customer, and had entered into a Memorandum of Understanding with another large customer.

As a consequence, the Eleventh Circuit concluded that *El Paso* guided its decision here. In both cases, the relevant market was highly concentrated. In both cases, the acquisition ensured a continuation of high concentration and eliminated the decrease that would result from the acquired company's entry. In both cases, the pre-acquisition market activity by the acquired company — although resulting in no actual sales — had a substantial and actual procompetitive effect on the market.

The court then relied upon the Supreme Court's subsequent characterization in *United States v. Marine Bancorporation, Inc.*, 418 U.S. 602 (1974) of *El Paso* as an actual competitor case to conclude that the *Philadelphia National* presumption could apply. Since, in the FTC's and Eleventh Circuit's views, Polypore could not overcome the presumption, the court held that the Commission correctly found that the merger violated Section 7 of the Clayton Act.

Polypore also argued that its and Microporous's product for deep-cycle batteries were not close competitive substitutes and should not be considered part of the same market, because of the disparity in price between the two products and the differences in quality. The Commission had relied upon the switch of several customers between the products to place them in same market. Applying the typical *Brown Shoe* factors for defining product markets, the court found that the Commission's finding should be upheld.

As to the divestiture remedy, Polypore challenged the inclusion of the Austrian plant. The FTC justified its inclusion to ensure that the Tennessee plant would have sufficient capacity to service the United States market and not have its capacity diverted for European customers. Recognizing the FTC's discretion on crafting a remedy, and invoking Supreme Court jurisprudence from the 1960s, *Ford Motor Co. v. United States*, 405 U.S. 562 (1972), and *United States v. E.I. DuPont De Nemours & Co.*, 366 U.S. 316 (1961), the court concluded that the remedial order was within the Commission's broad authority.

The Eleventh Circuit's decision never cites to or presents discussion of the Horizontal Merger Guidelines, even though it concludes it was reviewing a horizontal merger. Instead, it uses Supreme Court precedent that predates the issuance of the Guidelines. In doing so, it gives the FTC merger enforcement a positive endorsement and expands in today's world the situations where a "competitor" without sales can be considered an actual competitor.

Companies seeking safety in the black and white parameters of what constitutes a market participant should take note that even those lines can be blurred under the Clayton Act. Moreover, the Eleventh Circuit's leniency as to the FTC's power to craft remedies should be closely monitored.

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