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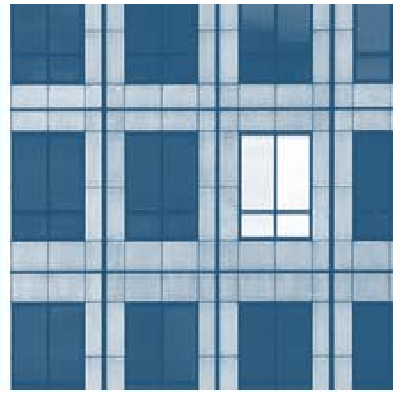
On the Subject



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The final revised Horizontal Merger Guidelines, which resemble the draft guidelines issued in April 2010, remain focused on actual competitive effects over technical market definition in determining the FTC's and DOJ's merger enforcement posture.

FTC and DOJ Issue Final Revised Horizontal Merger Guidelines

On August 19, 2010, the Federal Trade Commission (FTC) released the final revised Horizontal Merger Guidelines. The guidelines, first issued in 1992 and revised in 1997, describe the FTC and U.S. Department of Justice's (DOJ) methodology for analyzing the likely competitive impact of mergers and acquisitions (including partial acquisitions) between competitors. The final guidelines, which set out the agencies' current analytical framework in assessing the legality of proposed transactions, follow an earlier draft issued for public comment in April 2010. (See *On The Subject* titled "FTC and DOJ Issue Revised Horizontal Merger Guidelines for Comment" for more on the April guidelines at http://www.mwe.com/index.cfm/fuseaction/publications.nldetail/object_id/e779372f-5765-4dbf-a35c-9b3c70132e23.cfm)

A major theme of the revised guidelines is the agencies' expressed desire to have more flexibility in assessing whether a merger is likely to lessen competition by not committing to any one particular methodology. In practice, businesses contemplating transactions should not anticipate dramatic changes in merger analysis, but should expect a process that is both more rigorous and more fluid, depending on the types of evidence available to the parties and the agencies.

The Role of Market Definition Recast

The most significant change in the guidelines since 1992 is the de-emphasis of market definition and corresponding increased focus on the actual competitive effects that are likely to result as a consequence of the transaction. Under the old orthodoxy, market definition played a central role in measuring the likely competitive effects of a transaction. However, under the new methodology first advanced in the April draft, where evidence of competitive effects already exists, market definition is not as crucial to the merger analysis. Adverse competitive effects more directly address the central question of any merger analysis, which is whether the transaction may substantially lessen competition.

In the final revised guidelines, the FTC and DOJ further refine the role market definition plays in the agencies' analysis. In the April guidelines, the agencies explained that they "define relevant markets to help analyze the competitive effects of a horizontal merger." However, the final guidelines recast that role of market definition as germane only once the agencies "identify a potential competitive concern," at which point market definition serves two roles: specifying the line of commerce in which the competitive concern arises, and allowing the agency to identify market participants and measure shares and market concentration. Market definition historically has performed these functions in merger analysis, serving as the primary means for determining whether a transaction was likely to result in anticompetitive effects. However, the final guidelines relegate market definition to a supporting role in analyzing the impact of competitive concerns that have already been identified.

Other Changes From the April Guidelines

There are some other nominal changes between the April guidelines and the final guidelines. For example, the hypothetical monopolist test whereby the agencies test the boundaries of a market by analyzing whether purchasers would substitute a product in the face of a small but significant and non-transitory increase in price (SSNIP) survived from the 1992 guidelines. The April guidelines applied a 10 percent—instead of the prior 5 percent—SSNIP where explicit or implicit prices for the firm's contribution to value could be identified. The final guidelines eliminate that provision and simply rely on a 5 percent SSNIP, with the added caveat that the appropriate SSNIP to be applied may depend on the nature of the industry and the merging parties' positions within it.

When looking at potential unilateral competitive effects of a transaction (for instance, in a merger to monopoly), the April guidelines introduced the application of diversion ratios, which measure the fraction of unit sales diverted to a second product when the price of the first product increases. Diversion ratios may indicate the presence of upward pricing pressure on the first product as a result of the merger. Several informal comments noted that in almost any merger or acquisition there would be a diversion ratio of greater than zero, which, according to the April guidelines, would indicate some upward pricing pressure as a result of the merger. Seemingly in response to this concern and the suggestion of possible over-enforcement, the final guidelines note "[i]f the value of diverted sales is proportionately small, significant unilateral price effects are unlikely."

Conclusion

While the guidelines de-emphasize the role of market definition in the FTC's and DOJ's analyses of transactions, they largely memorialize the agencies' existing practices in the merger review process. The new shift in focus seems to be a response to the agencies' difficulties in sustaining their burden of proof concerning market definition in past unsuccessful merger challenges. By placing greater emphasis on evidence of a transaction's competitive effects, the agencies allow themselves more flexibility to avoid complicated market definition issues and instead address the central question posed by a transaction, namely whether it will result in anticompetitive effects. This means that parties will need to be prepared to marshal evidence on a broader range of potential issues in defending their proposed transactions. Evidence of competitive effects also will be critical to parties that have already consummated transactions, which, as the new guidelines make clear, remain subject to post-closing challenges.

From a practical perspective, the revised guidelines continue to emphasize the importance of the parties' ordinary course documents and customer opinions in the agencies' analyses. To minimize agencies' scrutiny of transactions, companies must continue to be careful about how they draft business and strategic plans in the ordinary course of business, as well as documents analyzing a proposed transaction. Overall, parties will need to exercise greater care in how they discuss and document competition and pricing decisions in internal documents. This also underscores the significance of the recently announced proposed changes to the Hart-Scott-Rodino (HSR) rules and form, which will require the submission of such documents with the parties' HSR filings. (See *On The Subject* titled "FTC Proposes Changes to Hart-Scott-Rodino Notification Rules and Form" at "http://mwe.com/index.cfm/fuseaction/publications.nldetail/object_id/29f0c636-f65e-4245-a7a4-aa8ae46973c5.cfm for our discussion on those changes.) In light of the heavy emphasis the new guidelines place on economic evidence, clients may consider engaging economic consultants earlier in the transaction planning process. Nevertheless, only time will tell how much weight courts will give the revised guidelines, especially given long-standing case law that calls for defining the relevant market as the first step in analyzing a transaction's likely competitive effects.

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