

**PUBLIC COMMENTS ON THE U.S. ANTITRUST AGENCIES' DRAFT VERTICAL MERGER GUIDELINES BY CLIFFORD CHANCE US LLP**

**February 26, 2020**

The much anticipated draft 2020 Vertical Merger Guidelines (“Proposed Guidelines”) jointly released for public comment by the Federal Trade Commission (“FTC”) and the Antitrust Division of the U.S. Department of Justice (“DOJ”) (together the “Agencies”) need certain revisions to achieve the stated goals. The purpose of the Proposed Guidelines is to update the analytical framework used by the FTC and DOJ to evaluate the competitive effects of vertical mergers. However, the Proposed Guidelines do not provide much detail to guide meaningfully businesses, practitioners, or courts.

The Proposed Guidelines are the first update of the analysis the Agencies apply to vertical mergers put forth in nearly four decades, and we commend this effort. However, as such, the Agencies should not miss the opportunity to provide greater clarity on the likely procompetitive benefits of vertical transactions, the analytical framework used to evaluate such combinations, and achieve consistency with other merger regimes outside the United States, while taking into consideration the impact of the “soft” 20 percent threshold set in the Proposed Guidelines could have on enforcement.

For example, the Agencies have long recognized that most vertical mergers are inherently procompetitive. In fact, the FTC’s Director of the Bureau of Competition recently affirmed that “overall there is a broad consensus in competition policy and economic theory that the majority of vertical mergers are beneficial because they reduce costs and increase the intensity of interbrand competition.”<sup>1</sup> More importantly, courts have routinely recognized that vertical mergers tend to be procompetitive.<sup>2</sup> We think it is important the Proposed Guidelines expressly acknowledge the procompetitive nature of most vertical transactions to set the context for the review of vertical transactions and that the analytical approach adopted is consistent with this reality.

While the Proposed Guidelines address the benefit of eliminating double marginalization, they fall short in providing explicit examples of other vertical merger specific efficiencies the Agencies recognize based on their “new economic understandings.” For example, the Agencies’ joint Horizontal Merger Guidelines<sup>3</sup> note that the Agencies:

have found that certain types of efficiencies are more likely to be cognizable and substantial than others. For example, efficiencies resulting from shifting production among facilities formerly owned separately, which enable the merging firms to reduce

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<sup>1</sup> D. Bruce Hoffman, Dir., Bureau of Competition, Fed. Trade Comm’n, Vertical Merger Enforcement at the FTC, Remarks Before the Credit Suisse 2018 Washington Perspectives Conference 8 (Jan. 10, 2018).

<sup>2</sup> See *United States v. AT & T Inc.*, 310 F. Supp. 3d 161, 197 (D.D.C. 2018), *aff’d sub nom. United States v. AT&T, Inc.*, 916 F.3d 1029 (D.C. Cir. 2019) (“Vertical mergers often generate efficiencies and other procompetitive effects.”); *Nat’l Fuel Gas Supply Corp. v. F.E.R.C.*, 468 F.3d 831, 840 (D.C. Cir. 2006) (“We began by emphasizing that vertical integration creates efficiencies for consumers.”); *Tenneco Gas v. FERC*, 969 F.2d 1187, 1197 (D.C. Cir. 1992) (“In a competitive market, the efficiencies of the pipeline-affiliate relationship should produce benefits for consumers.”); see also *Comcast Cable Comms., LLC v. FCC*, 717 F.3d 982, 990 (D.C. Cir. 2013) (Kavanaugh, J., concurring) (“[A]bsent market power, vertical integration and vertical contracts are procompetitive.”) (citing Douglas H. Ginsburg, Vertical Restraints: De Facto Legality Under the Rule of Reason, 60 *Antitrust L.J.* 67, 76 (1991)).

<sup>3</sup> U.S. DEP’T OF JUSTICE & FED. TRADE COMM’N, HORIZONTAL MERGER GUIDELINES (2010), <http://www.justice.gov/atr/public/guidelines/hmg-2010.pdf>.

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the incremental cost of production, are more likely to be susceptible to verification and are less likely to result from anticompetitive reductions in output. Other efficiencies, such as those relating to research and development, are potentially substantial but are generally less susceptible to verification and may be the result of anticompetitive output reductions. Yet others, such as those relating to procurement, management, or capital cost, are less likely to be merger-specific or substantial, or may not be cognizable for other reasons.

The Proposed Guidelines fail to outline, even at a high-level, the Agencies' "new economic understandings."

The Proposed Guidelines should provide insight into the types of evidence the Agencies will find sufficient to support efficiency arguments. The Proposed Guidelines should also examine recent vertical transactions, acting as natural experiments, to explore what the Agencies have learned about efficiencies in vertical mergers. Such examinations have often been part of any guidance issued by the Agencies. If the Proposed Guidelines delineate other types of persuasive efficiencies, beyond eliminating double marginalization, merging parties, attorneys, and economists can be better prepared to engage in more fruitful discussions earlier in the merger review process. Likewise, such guidance would help courts better understand how the Agencies consider economic arguments regarding efficiencies.

In addition, the Proposed Guidelines miss the opportunity to harmonize the Agencies' stated approach to vertical transactions with established guidance in other jurisdictions around the world. Most notably, the Proposed Guidelines indicate the Agencies will evaluate market shares and concentration—measured using the same methodology described in the long-standing Horizontal Merger Guidelines—but will not use these metrics as a "rigid screen." On that basis, the Proposed Guidelines establish a "soft" 20 percent threshold, where the Agencies are "unlikely to challenge a vertical merger" if the merging parties have less than a 20 percent share of the relevant market and the related product is used in less than 20 percent of the relevant market.

Consideration should be given on whether the 20 percent threshold should be aligned with other jurisdictions, most notably the European Commission. Under the European Commission's Guidelines on the Assessment of Non-Horizontal Mergers Under the Council Regulation on the Control of Concentrations Between Undertakings ("EC Guidelines"),<sup>4</sup> the Commission is "unlikely to find concern" with a vertical merger affecting less than 30 percent of the relevant markets and where the post-merger Herfindahl-Hirschman Index ("HHI") falls below 2000. Most European authorities have adopted a similar approach. The suggested 20 percent threshold in the Proposed Guidelines creates a discrepancy between the U.S. and the European Commission

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<sup>4</sup> GUIDELINES ON THE ASSESSMENT OF NON-HORIZONTAL MERGERS UNDER THE COUNCIL REGULATION ON THE CONTROL OF CONCENTRATIONS BETWEEN UNDERTAKINGS (Official Journal of the European Union) (2008), <https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2008:265:0006:0025:en:PDF>.

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causing unnecessary uncertainty within the business and legal communities and could lead to inconsistent enforcement outcomes across borders.<sup>5</sup>

Moreover, beyond the dangers created by a lack of international harmonization, setting the threshold at 20 percent may be unnecessarily low given the pro-competitive nature of most vertical mergers. The 20 percent threshold has the potential to capture many vertical transactions that would be considered only “moderately concentrated,” even potentially at the low end of the 1500 to 2500 HHI range. Moreover, “soft” thresholds have a tendency to “harden” over time. While the “soft” 20 percent thresholds in the Proposed Guidelines is explicitly not a safe harbor, it may turn out that, in practice, the provision could creep into in the territory of creating a danger zone for companies with shares above the threshold. Indeed, setting the threshold so low also fails to recognize the inherently procompetitive nature of the majority of vertical combinations.

While we commend the Agencies for taking this step to provide updated guidance on their analysis of vertical mergers, we hope that they may consider further elaboration on their thinking, which would be a step even further down the road toward assisting courts, businesses, and practitioners.

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<sup>5</sup> Both Japan and Chile have adopted thresholds similar to the European Commission. In Japan, a vertical merger is unlikely to restrain competition if either: 1) the combined entity’s market share is below 10 percent in all relevant markets, or 2) the post-merger HHI is below 2,500 and the combined entity’s market share is below 35 percent. In Chile’s Fiscalía Nacional Económica explained that for vertical mergers in the technology, media, and telecom sectors, a 30 percent market share is necessary to trigger heightened scrutiny.