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The Evolution of the FTC and DOJ Continues: Agencies Seek Public Comment on Draft Merger Guidelines

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The Federal Trade Commission (FTC) and the U.S. Department of Justice (DOJ) jointly issued new draft Merger Guidelines on July 19.[1] The draft Merger Guidelines were created with the goal “to better reflect how the agencies determine a merger’s effect on competition in the modern economy and evaluate proposed mergers under the law.” There are significant changes from the current guidelines both substantively and in form. These changes are consistent with the Biden administration agencies’ public statements and reflect the FTC’s and DOJ’s approach to merger investigations and enforcement actions over the last two years. The draft is subject to a 60-day comment period, which closes on September 18.

The changes come on the heels of the agencies’ proposal on June 27 to update the premerger notification form under the Hart-Scott-Rodino (HSR) Act. The proposed form update, the first of its kind in 45 years, would substantially increase the time, effort, and cost of making the filings of buyers and sellers.[2] The FTC notice estimates that HSR filings would require an average of 144 hours to prepare as compared to the current average of 37 hours. If the proposed changes are adopted, the FTC estimates that “complex” filings would require approximately 259 hours to complete. Many of the proposed changes appear to be aimed at providing substantial additional information related to the types of harm underlying the draft Merger Guidelines.

Broadly, the draft confirms the agencies’ interest in increased enforcement, particularly in tech and labor markets, decreased mergers, skepticism regarding merger-related efficiencies, concern for nascent competitors, distrust of “big” companies, and preference for organic growth.

To better understand the proposed changes to the Merger Guidelines, we highlight some of the most significant changes below.

- *Reducing the threshold for a presumption of anticompetitive effects*

Guideline 1 lowers the threshold for determining when a transaction results in a “highly concentrated market” to the level used by the guidelines issued in the 1980s and 1990s.Guideline 1 describes the use of the Herfindahl-Hirschman Index (HHI) to calculate market concentration. The HHI sums the squares of the market share of each competitor in the market. Under the 2010 merger guidelines, “[b]ased on their experience, the Agencies classif[ied] markets” with an HHI over 2,500, as “highly concentrated.” Transactions resulting in highly concentrated markets that involved an increase of more than 200 points were presumed to be likely to enhance market power.

Pursuant to draft Guideline 1, the agencies not only reduce the standard for a “highly concentrated” HHI to 1,800 from 2,500, but they also reduce the level of the post-transaction delta from 200 to 100. Accordingly, mergers in markets with HHIs greater than 1,800 and an increase of greater than 100 “causes undue concentration and triggers a structural presumption that the merger may substantially lessen competition or tend to create a monopoly.”

Another change is the addition of the “structural presumption” that mergers leading to a market share in excess of 30% are illegal.

- *Creating a dominance concept under U.S. law*

Dominance is not a concept enshrined in U.S. antitrust law but has been a part of merger analysis in Europe. Guideline 7 seeks to discourage any transaction that makes it harder for remaining competitors to compete. The guideline suggests a firm could be treated as “dominant” with a market share as low as 30%, and that transactions that might increase switching costs, interfere with use of competitive alternatives, deprive rivals of economies of scale, eliminate a nascent competitive threat, or “in any other way” entrench the combined firm’s position could be challenged. The agencies will view any merger involving a dominant firm with intense scrutiny.

- *Focus on mergers that “further a trend” toward market concentration*

Guideline 8 declares that the agencies will now scrutinize mergers in markets, which have been trending toward concentrated, and thereby the proposed transaction may substantially lessen competition. The guideline sets forth two factors to establish this trend: (1) if a market has shown a history of consolidation, such as a market with an HHI exceeding 1,000 and approaching 1,800, or (2) if the merger would increase the rate of concentration, such as increases in HHI over 200.

- *Adding examination of serial acquisitions as a whole*

Guideline 9 notes that the agencies have created another pathway to target mergers, which might, in the past, have evaded agency scrutiny, challenging a pending transaction based on past lawfully consummated mergers and company documents reflecting a strategy of growth through acquisition. Specifically, if either of the parties has a pattern or strategy of consolidation through acquisition, the agencies will examine the impact of the cumulative strategy to determine if that strategy may substantially lessen competition or tend to create a monopoly. If the agencies find that the strategy or acquisition history of a firm is suspect, they may combine multiple acquisitions for the purposes of their analysis of other indicia of lessening competition. Many interpret Guideline 9 as a reflection of skepticism of private equity transactions.

- *Suggesting increased enforcement of merger involving multisided platforms*

In another warning shot at the tech industry, the agencies made clear in Guideline 10 that anticompetitive effects on a single platform may make a merger illegal. The agencies view such platforms as markets themselves, and platform operators as having conflicts of interest to the extent they use their platform to sell products. Thus, a merger between a platform operator and a seller of goods who uses the platform will attract the attention of the agencies even if the merger would be totally innocuous if viewed only in the market of the products sold by the acquired seller.

- *Considering impacts on labor markets*

Guideline 11 confirms that the agencies will consider labor markets as they would other supply markets in analyzing mergers, where employers are competing buyers for labor. When assessing the degree to which the merging firms compete for labor, the agencies will consider whether the merger may result in lower wages or slowed wage growth, worse benefits or working conditions, or any other degradation of workplace quality.

- *Market definition: Considering bundling*

The agencies stated in an appendix detailing how they define markets that they will consider bundled products in a single relevant market, even if such conduct would not violate Section 2 of the Sherman Act. Bundling is conditioning the sale of a product in one market on the sale of a product in another market, or otherwise linking the sales of two products. By considering bundled products together, the agencies may be able to find that firms exceed the thresholds described above based on control of products outside the market directly affected by the transaction.

- *Efficiencies relegated to the appendix*

While the current guidelines explain how efficiencies may “enhance the merged firm’s ability and incentive to compete, which may result in lower prices” and other consumer benefits, the proposed guidelines are less clear on the impact of efficiencies to the agencies’ analysis. This section begins with a quote from *United States v. Philadelphia Nat’l Bank* that “possible economics [from a merger] cannot be used as a defense to illegality.” 374 U.S. 321, 371 (1963). It goes on to identify certain “cognizable efficiencies,” which “must be of sufficient magnitude and likelihood” to “prevent the creation of a monopoly.”

In sum, the draft Merger Guidelines should provide greater transparency to businesses considering acquisitions and enshrine evolving FTC and DOJ policies which have increased the risk of merger investigations and enforcement actions under the current administration.

The public has been invited to comment on the draft Merger Guidelines. If you have any questions, comments, or concerns about the proposed changes and its implications, Troutman Pepper’s Antitrust attorneys are available to guide you through these issues and evaluate the best strategy for your business.

APPENDIX OF SIGNIFICANT FORM CHANGES

- *Parties*. Identification of entities within the ultimate parent entity (UPE) or acquired entity, minority shareholders, and other noncontrolling entities, and create new requirements to identify certain other interest holders that may exert influence, as well as officers, directors, and board observers.

- Organize the list of entities held by the UPE or acquired entity by operating company, and for each such operating company or business, provide d/b/a(s) and f/k/a(s) within the three years preceding filing.

- For the acquiring UPE, report minority holders of (1) the acquiring entity, (2) any entity directly or indirectly controlled by the acquiring entity, (3) any entity that directly or indirectly controls the acquiring entity, and (4) any entity within the acquiring person that has been or will be created in contemplation of, or for the purposes of, effectuating the transaction. For entities affiliated with a master limited partnership, fund, or investment group, the "doing business as" or "street name" of that group would also be required.

- For the acquiring UPE, identify certain individuals (other than employees) or entities that, in relation to the acquiring entity or any entity it directly or indirectly controls or is controlled by, who (i) provide credit in conjunction with or result of the transaction, provided credit totaling 10% or more of the value of the entity; or (ii) are holders of nonvoting securities, warrants, or options would be limited to those the value of which equals or exceeds 10% of the entity or could be converted to 10% or more of the voting securities or noncorporate interests of the company.

- *Officers, Directors, and Board Observers*. Identify the officers, directors, and board observers (or in the case of unincorporated entities, individuals exercising similar functions) of the acquired entity(s) and entities within acquiring person(s), as applicable, for the prior two years, and for each individual, identify any other companies for which those individuals would serve or have served during the prior two years as officers, directors, or board observers. Provide the same information for the prospective officers, directors, or board observers of the acquired and acquiring entities after the transaction, as well as for any officers, directors, or board observers of new entities created as a result of the transaction (and, in each case, for unincorporated entities, individuals serving those functions). If it would be impossible to identify the specific officers, directors, and board observers, filers should describe who would have the authority to choose them.

- *Transaction Information*. The acquiring UPE will be required to briefly describe the business operations of all entities within the acquiring person to provide a clear overview of all aspects of the acquiring person's pre-transaction business.

  - The acquiring and acquired person will be required to submit a narrative describing all strategic rationales for the transaction, including, those related to competition for current or known planned products or services that would or could compete with a current or known planned product or service of the other reporting person, expansion into new markets, hiring the sellers' employees (so-called acqui-hires), obtaining certain intellectual property, or integrating certain assets into new or existing products, services, or offerings. Also, identification of which documents submitted with the HSR filing support the rationale(s) described in the narrative.

- Provide a diagram of the deal structure along with a corresponding chart that would explain the relevant entities and individuals involved in the transaction.

- *Agreements and Timeline*. Require filing persons to produce (i) all agreements, inclusive of schedules, exhibits, and the like, that relate to the transaction, regardless of whether both parties to the transaction are signatories; (ii) all agreements between any entity within the acquiring person and any entity within the acquired person in effect at the time of filing or within the year prior to the date of filing, including but not limited to, licensing agreements, supply agreements, noncompetition or nonsolicitation agreements, purchase agreements, distribution agreements, or franchise agreements; and (iii) narrative timeline of key dates and conditions for closing.

- *Competition and Overlaps*. In addition to the transaction-related documents currently required under Item 4(c) and 4(d) prepared by or for officers and directors, filing persons would also need to submit (i) documents prepared by or for supervisory deal team lead(s) and (ii) drafts of responsive transaction-related documents if that document was provided to an officer, director, or supervisory deal team lead(s).

  - *Periodic Plans and Reports*. Submission of (i) semi-annual and quarterly plans and reports that discuss market shares, competition, competitors, or markets of any product or service that is provided by both the acquiring person and acquired entity, if those documents were shared with a chief executive of an entity involved in the transaction, or with certain individuals who report directly to a chief executive; and (ii) all plans and reports submitted to the board of directors (or, in the case of unincorporated entities, individuals exercising those functions) that discuss market shares, competition, competitors, or markets of any product or service that is provided by both the acquiring person and acquired entity.

  - Submission of an organizational chart(s) reflecting the position(s) within the filing person's organization held by identified authors, and for privileged documents, the recipients of each document submitted with the HSR filing. Identification of the individuals searched for responsive documents.

- *Competition Analysis*. Each filing person would be required to list each current or known planned product or service that competes with (or could compete with) a current or known planned product of the other filer. For each such overlapping product or service, the filing person would provide sales, customer information (including contacts), a description of any licensing arrangements, and any noncompete or nonsolicitation agreements applicable to employees or business units related to the product or service.

- *Supply Relationships*. Filing persons would report (i) sales to the other filing person and to any other business that, to the best of the filing person's knowledge, uses its product, service, or asset as an input for a product or service that competes or is intended to compete with the other filing person's products or services; (ii) information (including contact information and a description of the supply agreement) for other customers that use the product, service, or asset to compete with other filing person; (iii) similar information for purchases made from the other filing person and from any other business that, to the best of the filing person's knowledge, competes with the other filing party to provide a substantially similar product, service, or asset.

- *Labor Markets*. Filers would need to classify their workers into occupational categories based on the Standard Occupational Classification (SOC) system, list the five largest categories of workers by the relevant six-digit SOC classification, provide the total number of employees for each six-digit code identified, and identify any penalties or findings that were issued against the acquiring person or acquired entity by the U.S. Department of Labor's Wage and Hour Division, the National Labor Relations Board, or the Occupational Safety and Health Administration during the five-year period before the filing.
    - For each of the five largest SOC codes in which both parties employ workers, the filing persons would be required to list the overlapping Economic Research Service's Commuting Zones from which the employees commute and the total number of employees within each commuting zone.

- *NAICS Information*. Filing persons would need to (i) list every NAICS code that describes the products or services offered and use end notes as needed to clarify selections and any potential overlap where the same revenues are reported in more than one NAICS code; (ii) require acquiring persons and acquired entities with more than one operating company or unit to identify which entity(s) derives revenue in each code; (iii) acquiring person would be required to identify any NAICS codes for products and services under development if those codes would overlap with the codes for current or known pipeline products or services of the acquired entity(s); and (iv) acquired person would identify the NAICS codes that would apply to the products or services of the acquired entity(s) that are under development or pre-revenue and anticipated to have annual revenue totaling more than $1 million within the following two years.

- *Minority-Held Entity Overlaps*. List all the minority-held entities of the acquiring person and its associates or acquired entity (as appropriate) and proposes once again to require identification of those that, to the filing person's knowledge or belief, would derive revenue in the same NAICS codes or have operations in the same industry as the other filing person.

- *Prior Acquisitions*. Both the acquiring person and the acquired entity will be required to provide information about prior acquisitions for the previous 10 years and eliminate the threshold for listing prior acquisitions, which currently limits reporting to only acquisitions of entities with annual net sales or total assets greater than $10 million in the year prior to the acquisition.

- *Foreign Subsidies.* Persons making an HSR filing would be required to disclose information about foreign subsidies from countries or entities that threaten U.S. strategic or economic interest.

- *Defense Information*. Both the acquiring and acquired person would identify whether they have existing or pending defense or intelligence procurement contracts, as defined by 10 U.S.C. 101(a)(6) and 50 U.S.C. 3033(4), valued at $10 million or more, and provide identifying information about the award and relevant DoD or IC personnel.

- *Document Preservation*. Filers would need to identify and list all communications systems or messaging applications on any device used by the acquiring or acquired person (as appropriate) that could be used to store or transmit information or documents related to its business operations and affirm that all necessary steps have taken to prevent destruction of documents and information related to the transaction, include suspension of auto-deletion protocols.

- *Foreign Filings.* Require parties to identify the foreign jurisdictions where each has already filed or is preparing notifications to be filed as well as a list of the jurisdictions where it has a good faith belief it will file.

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[1] The first merger guidelines were issued by the DOJ, Antitrust Division, in 1968. Different iterations of have been revised and refined in 1982, 1984, 1992, 1997, and 2010.

[2] A summary of many of the key changes to the form is provided as an appendix here.

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