Merger Review

Antitrust
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Initial observations

- There's surprisingly little case law on mergers.
- What's interesting mostly has to do with what mergers the government agencies (i.e., DOJ or FTC) decide to challenge.
- And if there's a challenge, resolving it will mostly be about applying DOJ/FTC's own guidelines. It's not about statutory text. It's not really about case law either.
- The analysis comes down to considering anticompetitive effects, procompetitive virtues, and redeeming efficiencies.
  - (And from a law-student perspective, those concepts can be learned from the case law in non-merger Sherman Act § 1 & § 2 cases.)

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  - (A… epts ca… merger Sher… § 2 cases.)

This is why merger analysis is not typically an emphasis of an antitrust course. That's despite the fact that when a lot of people hear "antitrust law" they think of mergers and challenges to mergers.

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But there are at least a few things worth pointing out about merger review. So that's what we'll do here.

Economics and Structure

Kinds of mergers

- Horizontal mergers
- Vertical mergers
- Conglomerate mergers

Potential benefits of mergers

- All kinds of efficiencies
- Economies of scale
- Preserving firms that would fail
- The list is endless ...

Potential problems with mergers

- Unilateral effects – market/monopoly power of the merged firm
- Oligopoly effects – concentration of a market that can cause prices to increase, either through:
  - purely self-interested/independent decision-making of firms, *or*
  - oligopolistic coordination (e.g., legal “conscious parallelism”)
- According to research, five significant firms in a market tends to be enough to prevent oligopolistic coordination

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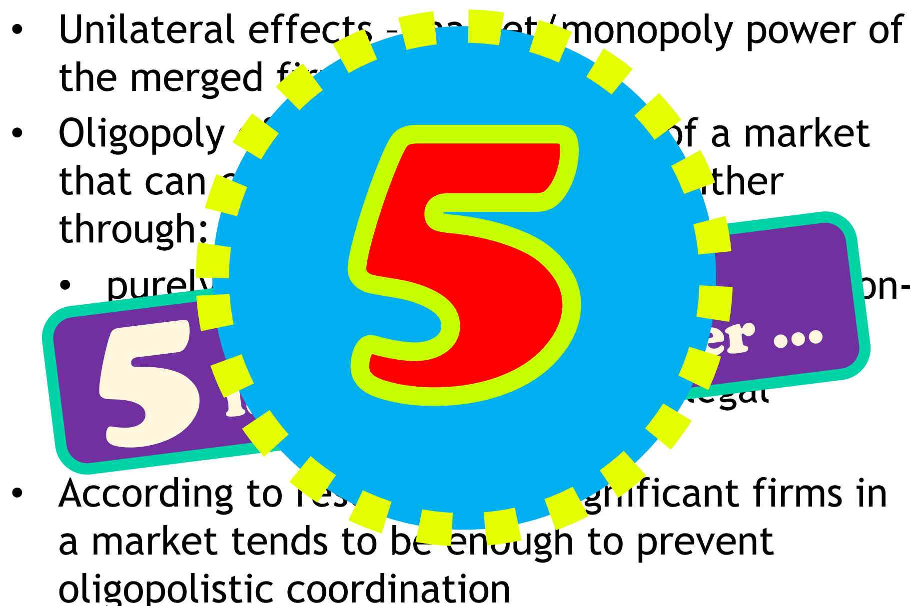


Quick question:

According to market research, how many sellers of significant size are generally sufficient to avoid oligopolistic coordination?

Qui question:

According esearch, how many sel ant size are generally su to avoid oligopolisti dination?

Legal Structure for Merger Review

Applicable law

- Mergers and acquisitions can be challenged under Sherman Act § 1 or § 2, or FTC Act § 5, but generally they are challenged under the Clayton Act § 7.
- Clayton Act § 7 allows the blocking of mergers and acquisitions where "the effect of such ... may be to substantially lessen competition, or tend to create a monopoly."

Hart-Scott-Rodino Act

15 USC § 18a

Per-merger filing with DOJ/FTC is required where:

- the stock acquisition value exceeds $50M <u>and</u> the acquirer and target have assets or annual sales in excess of $10M for one and $100M for the other (either way), <u>OR</u>
- the stock acquisition value exceeds $200M

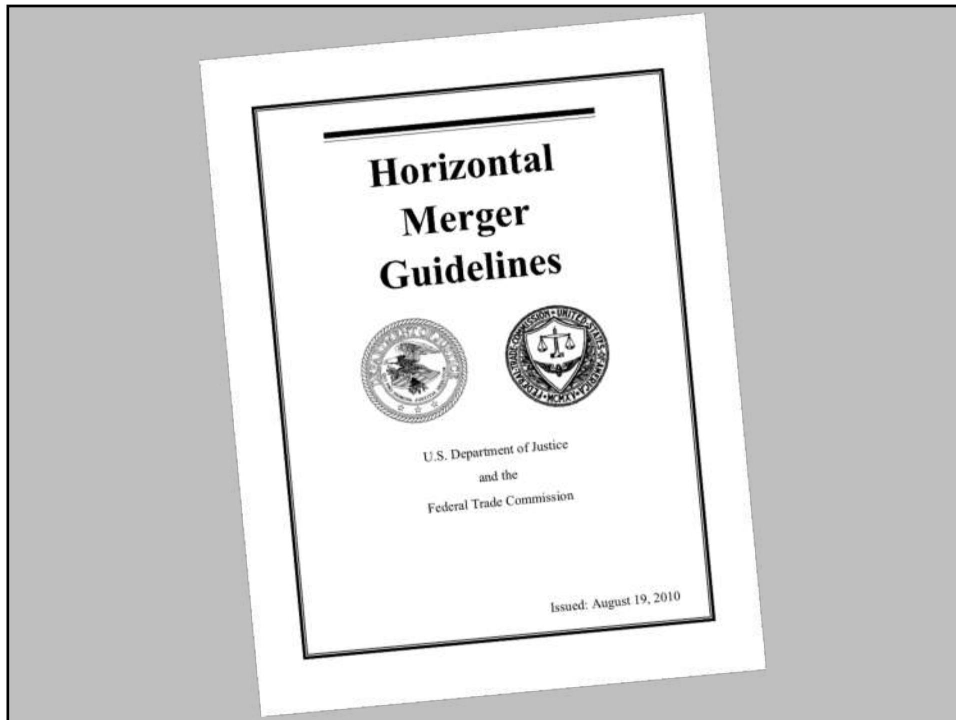
Amounts are in 2004 dollars.

There's a passive investor exception.

DOJ/FTC challenge

- DOJ and FTC split up merger reviews between them.
- After the HSR filing, the agency has 30 days in which to make a “second request” for additional information (15 days for cash tender offers).
  - This happens about 5% of the time.
- The agency then engages in a detailed analysis.
  - Third parties can weigh in.
- To avoid adverse effects on competition, the merging firms can offer to divest themselves of certain assets or bind themselves to certain conduct.
- Often a merger dies if the agency opposes the merger.
- If the agency is opposed and the merging parties want to forge ahead, the dispute goes to court.
- Courts tend to evaluate mergers largely by the DOJ/FTC guidelines(!).

Substance of Merger Review



from the Horizontal Merger Guidelines:

- "The Agencies seek to identify and challenge competitively harmful mergers while avoiding unnecessary interference with mergers that are either competitively beneficial or neutral."
- "The unifying theme of these Guidelines is that mergers should not be permitted to create, enhance, or entrench market power or to facilitate its exercise."
- "The Agencies consider any reasonably available and reliable evidence to address the central question of whether a merger may substantially lessen competition."
- "[A] primary benefit of mergers to the economy is their potential to generate significant efficiencies and thus enhance the merged firm's ability and incentive to compete, which may result in lower prices, improved quality, enhanced service, or new products."
- The Agencies will not challenge a merger if cognizable efficiencies are of a character and magnitude such that the merger is not likely to be anticompetitive in any relevant market.

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So, in other words, balance the expected anticompetitive effects, procompetitive virtues, and redeeming efficiencies.

One thing that is interesting about the Horizontal Merger Guidelines is their use of the “HHI index” ...

HHI index

- The Agencies often calculate the Herfindahl-Hirschman Index ("HHI") of market concentration.
- The HHI is calculated by summing the squares of the individual firms' market shares and thus gives proportionately greater weight to the larger market shares.
- For example, a market consisting of four firms with market shares of 30%, 30%, 20%, and 20%, has an HHI of

– from the Horizontal Merger Guidelines

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- For example, a market consisting of four firms with market shares of 30%, 30%, 20%, and 20%, has an HHI of 2600.

$$30^2 + 30^2 + 20^2 + 20^2$$
$$= 900 + 900 + 400 + 400$$
$$= 2600$$

– from the Horizontal Merger Guidelines

HHI index

Question:

What would be the HHI of a 100% pure monopoly?

100^2

$= 10,000$

HHI index

- The HHI ranges from 10,000 (in the case of a pure monopoly) to a number approaching zero (in the case of an atomistic market).
- Although it is desirable to include all firms in the calculation, lack of information about firms with small shares is not critical because such firms do not affect the HHI significantly.

– from the Horizontal Merger Guidelines

HHI index

The agencies generally classify markets into three types:

- Unconcentrated Markets: HHI below 1500
- Moderately Concentrated Markets: HHI between 1500 and 2500
- Highly Concentrated Markets: HHI above 2500

– from the Horizontal Merger Guidelines

HHI index

The agencies generally classify markets into th… … below 1500 … rkets: HHI … HHI above

But wait!! How do we define the *market*?!?

– from the Horizontal Merger Guidelines

HHI index

The agencies generally [...]ify markets into th[...]

- [...] below 1500
- [...]kets: HHI
- [...]

But wait!! How do we define t[...]

You got this! ☺

The same way as for monopoly analysis! ☺

– from the Horizontal Merger Guidelines

Let's try a problem …

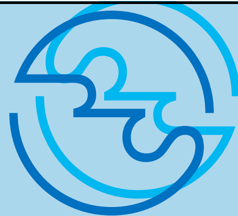
HHI index

The agencies employ the following general standards for the relevant markets they have defined:

- Small Change in Concentration: Mergers involving an increase in the HHI of less than 100 points are unlikely to have adverse competitive effects and ordinarily require no further analysis.
- Unconcentrated Markets: Merger… are u… further
- … 100 … rant s…
- H… markets: Mergers resulting in highly concentrated markets that involve an increase in the HHI of between 100 points and 200 points potentially raise significant competitive concerns and often warrant scrutiny. Mergers resulting in highly concentrated markets that involve an increase in the HHI of more than 200 points will be presumed to be likely to enhance market power. The presumption may be rebutted by persuasive evidence showing that the merger is unlikely to enhance market power.

– from the Horizontal Merger Guidelines

We'll apply all of this stuff …



sky lasso

Sky Lasso with 10% of the market wants to buy Acme Aviation Services with 15% of the market. The current market will go
from 10%, 15%, 20%, 25%, 30%
to 25%, 20%, 25%, 30%.

Will the merger pass agency scrutiny?

$10^2+15^2+20^2+25^2+30^2$
$= 100+225+400+625+900$
$= 2250$ pre-merger

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increase of 300

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- Moderately Concentrated Markets: HHI between 1500 and 2500 ← before
- Highly Concentrated Markets: HHI above 2500 ← after

from moderately concentrated to highly concentrated

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2550 post-merger
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- from the Horizontal Merger Guidelines

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- ~~Moderately Concentrated Markets: Mergers resulting in moderately concentrated markets that involve an increase in the HHI of more than 100 points potentially raise significant competitive concerns and often warrant scrutiny.~~ ← no, it's more than that
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So this is an example of how ...

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Vertical mergers (1/2)

- Lots and lots of efficiencies ...
- Some examples of possible anticompetitive effects:
  - Creating a need for two-level entry
  - Facilitating horizontal collusion ...
    - If upstream firms integrate retail, they can monitor each other's prices for a cartel
    - By eliminating a disruptive buyer that pushes upstream firms to cheat on their cartel

Vertical mergers (2/2)

- "[A]ctual U.S. enforcement action against vertical mergers is nearly non-existent." Elhauge (EE^{3d} at 796)
- In June 2020, DOJ and FTC released new Vertical Merger Guidelines (first update since 1984).
- The new Guidelines document:
  - Says "vertical mergers often benefit consumers" but are "not invariably innocuous"
  - Calls for analyzing anticompetitive effects, procompetitive virtues, and redeeming efficiencies.
  - Offers no bright line rules.
  - References the Horizontal Merger Guidelines.