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November 1, 2005

VIA E-MAIL

Andrew J. Heimert
Executive Director and General Counsel
Antitrust Modernization Commission
1120 G Street, N.W.
Suite 810
Washington, DC 20005

Re: Comments Concerning Antitrust Merger Enforcement

Dear Mr. Heimert:

Please find attached my statement concerning Antitrust Merger Enforcement, prepared for the November 17 hearing on that topic.

I am pleased to have the opportunity to participate and look forward to the Commission's questions and comments.

Best regards.

Sincerely,

James F. Rill

Enclosure

Written Statement of James F. Rill and Christopher J. MacAvoy Concerning Antitrust Merger Enforcement Before the Antitrust Modernization Commission[1]

Submitted October 31, 2005

This paper addresses the question under headings A and B posed by the Commission in its May 19, 2005 request for comments. In particular, the focus is whether the *Merger Guidelines*[2] provide adequate and effective guidance for the merger enforcement program and the collateral question whether there is adequate transparency in federal enforcement policy.[3]

Both questions are answered in the affirmative; however, the advances in these respects are evolutionary and continuing. Revision of the *Merger Guidelines* is not called for, and legislation in this area is neither necessary nor desirable.

I. INTRODUCTION

The *Merger Guidelines* provide a sound analytical path for merger enforcement and, as such, have been widely recognized and accepted. Although the 1968 ("Turner") *Merger Guidelines*[4] actually relaxed the strict, drastically low, and stultifying effect of leading Supreme Court decisions,[5] they were rigidly structural and provided little encouragement to would-be

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[2] U.S. Department of Justice and Federal Trade Commission, *Horizontal Merger Guidelines* (1992, revised 1997), reprinted in 4 TRADE REG. REP. (CCH) ¶ 13,104 [hereinafter, *Merger Guidelines*; reference to merger guidelines issued prior to 1992 will be distinguished by the year of issuance].

[3] 70 FED. REG. 28902-07 (May 19, 2005).

[4] Department of Justice, *Merger Guidelines* (1968), reprinted in 4 TRADE REG. REP. (CCH) ¶ 13,101.

[5] *United States v. Von's Grocery Co.*, 384 U.S. 270, 301, 86 S. Ct. 1478, 16 L. Ed. 2d 555 (1966); *United States v. Pabst Brewing Co.*, 384 U.S. 546, 86 S. Ct. 1665, 16 L. Ed. 2d 765 (1966).

merging competitors. The 1982 *Merger Guidelines*,[6] while remaining rooted in structural analysis, rejected the preexisting virtual *per se* approach and introduced the importance of competitive effects and entry. As such the 1982 *Merger Guidelines* were a fundamental turning point in merger enforcement.

The 1992 *Merger Guidelines* expanded the analytical flow of the 1982 *Merger Guidelines* by introducing the concept of uncommitted entry (supply response), clarifying the role of market concentration in creating a presumption that both provides a safe harbor and an analytical route for going forward once outside the safety zone, adding detailed factors to be considered in competitive effects assessment, including addition of the concept of unilateral effects, providing for a richer approach to the assessment of committed entry, and modestly expanding the scope of the efficiencies analysis. In addition, and importantly, the 1992 *Merger Guidelines* were the first to be issued jointly by the U.S. Department of Justice and the Federal Trade Commission.[7]

The *Merger Guidelines* have come under criticism in recent years on several grounds: 1) they preserve the "fiction" of relevant-market definition;[8] 2) the competitive effects section provides nothing more than an unstructured, unweighted checklist;[9] 3) the unilateral effects section is a variation on the historic submarket concept and is susceptible to the mischief of loose analysis and type one errors;[10] and 4) the efficiency section is too narrow and incomplete.[11]

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[6] Department of Justice, *Merger Guidelines* (1982), reprinted in 4 TRADE REG. REP. (CCH) ¶ 13,102.

[7] In 1982, the Federal Trade Commission issued an enforcement statement which conveyed very little guidance. Federal Trade Commission, *Statement of Federal Trade Commission Concerning Horizontal Mergers* (1982).

[8] *See* Jonathan B. Baker, *Product Differentiation Through Space and Time: Some Antitrust Policy Issues*, 42 ANTITRUST BULLETIN 177.

[9] *See* David T. Scheffman and Mary Coleman, *Quantitative Analyses of Potential Competitive Effects from A Merger*, June 9, 2003, available at www.ftc.gov/be/quantmergeranalysis.pdf.

[10] 4 Phillip E. Areeda, Herbert Hovenkamp & John L. Solow, ANTITRUST LAW ¶ 914a; Roscoe B. Starek, III, & Stephen Stockum, *What Makes Mergers Anticompetitive?: "Unilateral Effects" Analysis Under the 1992 Merger Guidelines,* 63 ANTITRUST L.J. 801, 814-15.

[11] *See, e.g.*, *Roundtable Conference with Enforcement Officials*, 65 ANTITRUST L.J. 929, 943-51 (1997).

Although these observations may have some kernel of validity, they are marginal criticisms that misjudge the flexibility of the *Merger Guidelines* to adapt to changes in industry dynamics and evolving economic and institutional learning, and, equally important, the degree to which they have been accepted by the agencies and the courts.

In a landmark 2003 article, then Federal Trade Commission Chairman Timothy Muris set forth the fundamental principles for a sound and widely accepted merger analytical platform. In summary, the elements were: clarity so as to be understood by courts, parties, and agency staffs; roots in sound economic and legal doctrine; and flexibility to adapt to evolving economic and legal learning.[12] Although perhaps the *Merger Guidelines* do not perfectly match the Muris principles, they come very close and provide a working tool for continued adaptation.

The fact is various programs are underway to shape and illuminate the *Merger Guidelines* framework. Most promising is the joint FTC-DOJ guideline implementation project, which appears designed to describe publicly the manner in which the *Merger Guidelines* have been applied in agency practice.[13] Also of interest on an international scale is the undertaking by a working group of the International Competition Network to review guidelines implementation by various member state enforcement agencies.[14]

II. THE MERGER GUIDELINES HAVE ACHIEVED WIDESPREAD ACCEPTANCE

Particularly since 1992, the *Merger Guidelines* have been cited by the U.S. courts with approbation as an appropriate analytical basis for case analysis. The *Merger Guidelines*'

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12 Timothy J. Muris, *Improving the Economic Foundations of Competition Policy*, 12 GEO. MASON LAW REV. 1 (2003).

13 Deborah Platt Majoras, Chairman, Federal Trade Commission, *Looking Forward: Merger and Other Policy Initiatives at the FTC*, Remarks before the ABA Antitrust Section Fall Forum, Washington, D.C., November 18, 2004.

14 International Competition Network Merger Working Group, *Merger Review Laws, Related Materials, and Templates*, available at www.internationalcompetitionnetwork.org/mergercontrollaws.html.

methodology has been cited with approval in a large number of court decisions over the past decade.[15] Cases expressly or tacitly endorsing the *Merger Guidelines*' approach include:

United States v. Sungard Data Systems, Inc., 172 F. Supp. 2d 172, 182 (D.D.C. 2001);

United States v. Swedish Match, 131 F. Supp. 2d 151, 160 (D.D.C. 2001);

FTC v. Staples, Inc., 970 F. Supp. 1066, 1076 (D.D.C.1997);

FTC v. Arch Coal, Inc., 329 F. Supp. 2d 109, 121, 123-131, 145-456, 150 (D.D.C. 2004);

FTC v. H. J. Heinz Co., 246 F. 3rd 708, 718, 720 (D.C. Cir. 2001)

United States v. Oracle Corp., 331 F. Supp. 2d 1098, 1109, 1131 (N.D. Cal. 2004)

FTC v. Cardinal Health, Inc., 12 F. Supp. 2d 34, at 45 (D.D.C. 1998);

United States v. Englehard Corp, 970 F. Supp. 1463, 1466 (M.D. Ga.), aff'd, 126 F. 3rd 1302 (11th Cir. 1997).

Moreover, the analytical path of the *Merger Guidelines* has been generally consistent with guidelines adopted in other jurisdictions. The Canadian Bureau of Competition Policy was pursuing a parallel track in developing horizontal merger guidelines at the same time the 1992 U.S. revisions were being developed. The staffs of the Department of Justice and the Bureau were in detailed consultation involving the approach and terms of their respective undertakings. Issued in 1991 and substantially revised in 2004, the analytical outline of the Canadian Guidelines is similar in many respects to that followed in the U.S.[16] The European Union's horizontal merger guidelines, also developed with consultative input from the U.S., follow the same general path of merger review.[17] A number of national competition agencies have

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15 A leading observer who participated in the development of the 1992 *Merger Guidelines* concludes: "Merger analysis at the federal antitrust agencies under the current guidelines is similar to the modern approach of the courts." Jonathan B. Baker, *Mavericks, Mergers, and Exclusion: Proving Coordinated Competitive Effects Under the Antitrust Laws*, 77-1 N.Y.U. L. REV. 135, at 151.

16 Canada, Competition Bureau, Director of Investigation and Research, *Merger Enforcement Guidelines* (March 1991, revised September 2004).

17 *Guidelines on the Assessment of Horizontal Mergers Under the Council Regulation on the Control of Concentrations Between Undertakings*, OFFICIAL JOURNAL OF THE EUROPEAN UNION (C 31, 5.2.2004).

developed horizontal merger guidelines which follow to a greater or lesser degree a consistent route.[18]

Although this point does not require a citation, it is at least worthy of note that the enforcement agencies also rely on *Merger Guidelines*' analysis in explaining their resolution of horizontal merger matters.[19]

III. GUIDELINE APPLICATION TO SPECIFIC AREAS OF ANALYSIS

A. Product Market Definition and Concentration

Some commentators have asserted that the relevant market definition protocol, as described in the *Merger Guidelines* is at worst unreal or at best somewhat dated.[20] To be sure, the *Merger Guidelines*' approach to product market definition is a proxy for direct measurement of the competitive proximity of the parties and the business of other candidates for inclusion in measurement of competitive effect. Some agency and private sector economists have urged that direct measurement of competitive effects by econometric techniques is a superior approach.[21] This argument has theoretical merit, but there are, at present, serious impediments to practical implementation; chiefly, a lack of sufficient confidence in the methodology or reliability of the underlying data, which calls for caution in relying on econometrics.[22] Nor is there sufficient

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[18] International Competition Network Merger Working Group, *Project on Merger Guidelines, Report for the Third ICN Annual Conference in Seoul, April 2004*, available at www.internationalcompetitionnetwork.org/seoul.pdf.

[19] *See, e.g.*, *Statement of the Federal Trade Commission Concerning Royal Caribbean Cruises, Ltd./P&O Princess Cruises plc and Carnival Corporation/P&O Princess Cruises plc*, FTC File No. 021 0041, available at http://www.ftc.gov/os/2002/10/cruisestatement.htm.

[20] *See, e.g.*, Gregory J. Werden, *Market Definition Under the Merger Guidelines: A Tenth Anniversary Retrospective*, ANTITRUST BULLETIN 517, 535.

[21] *See* Gregory J. Werden & Luke M. Froeb, *Simulation as an Alternative to Structural Merger Policy in Differentiated Products Industries*, in THE ECONOMICS OF THE ANTITRUST PROCESS: TOPICS IN REGULATORY ECONOMICS (Malcolm Coate & Andrew Kleit eds., 1996).

[22] Ken Heyer, *A World of Uncertainty: Economics and the Globalization of Antitrust*, 72 ANTITRUST L.J. 375. ("To incorporate perfectly into one's analysis uncertain costs and benefits, one would require an extraordinary amount of information on the distribution of possible outcomes. Complete information of this sort will never be available in an actual

clarity to achieve judicial understanding of the approach, particularly as it embraces simulation. Thus, the abandonment of the product market approach of the *Merger Guidelines* is unwarranted.[23]

Simulation techniques can be employed, nevertheless to test the results of analysis based on empirical evidence. The *Swedish Match* decision is instructive. There, the district court lacked sufficient confidence in the econometric simulations submitted by the parties to rest its relevant market conclusion on this evidence alone. Instead, the court looked to and found persuasive customer testimony, the parties' internal documents, outside research studies, relative price movements, and competitor testimony.[24]

Econometric simulation can be effective to test the conclusion reached by empirical evidence, and many commentators who are generally supportive of this technique endorse such deployment. Even economists who are enthusiastic about simulation analysis have stressed the evolutionary nature of the analytics, the need for further development, and the desirability of the agencies and the parties cooperating in furtherance of refinement and clarification.[25] The product market definition provision has also been criticized for leading to a first-cut rigidity of

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investigation. Nevertheless, the alternative of using an entirely wrong framework is likely to be worse than doing the best one can with imperfect information. Indeed, this scenario appears eerily comparable to the old joke about the man who is looking for a lost item under a street lamp, not because the item was lost there, but rather because the light is better.")

[23] In addition, judicial comfort with the guidelines approach further militates in favor of its retention, at least for the present. *See, e.g. FTC v. Staples, Inc.*, 970 F. Supp. 1066, 1078 (D.D.C. 1997); *Swedish Match*, 131 F. Supp. 2d 151, 160; *New York v. Kraft Gen. Foods, Inc.*, 926 F. Supp. 321 (S.D.N.Y. 1995).

[24] *Swedish Match,* at 162-165.

[25] *See, e.g.*, statements of Robert A. Willig and Dennis Carlton, Department of Justice and Federal Trade Commission Merger Workshop, 123-125, 134-135 (Feb. 19, 2004); Roundtable Discussion: *Unilateral Effects Analysis After Oracle*, 19 ANTITRUST 8, *inter alia* (Spring 2005) ("Simulation is a potentially useful tool, but it is just one element of the information set that we rely upon when deciding whether or not to recommend a case," Michael Vita, at 12; "Properly modified simulation models can deal very nicely with bargaining, negotiations and price discrimination, but testing the robustness and reliability of these models is complex . . ." Carl Shapiro, at 13.); Mary Coleman, *Key Issues in Proving Unilateral Effects After Oracle*, 19 ANTITRUST 26, 28 (Spring 2005) ("Simulation models are best considered as a potential means of summarizing the available empirical evidence.")

analysis and possibly to both error and an excessive weighting of market concentration.[26] Analysis under the *Merger Guidelines*, however, is not a rote march through a checklist, but a continuing process in which each area of analysis can be informed by another and modified as appropriate. Moreover, even where product market lines are drawn, the competitive effect of products outside the market can be taken into account to weaken further the concentration presumption.[27]

The 1992 *Merger Guidelines* retained the HHI metrics developed in 1982, but substituted the element of presumption at the highly concentrated level for the previous indication of likelihood of government challenge.[28] This change abandoned the litigation focus of prior versions and, more importantly, made clear that the higher post-merger concentration level did not suggest a "guideline violation" but rather dictated the need for further analysis of competitive effects, committed entry, and efficiency. In short, the presumption was designed to stimulate the further analysis, not supplant it.

To this effect, the 1992 *Merger Guidelines* were anticipated, and to some extent incentivized, by the *Baker Hughes* decision, which approved a merger on the basis of competitive effects and entry analysis, notwithstanding very high concentration based on current sales.[29] Subsequent court decisions, taking into account the *Merger Guidelines*, have acknowledged the limited weight to be accorded concentration and grounded analysis on other guidelines factors particularly competitive effects and entry.[30]

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26 *E.g.*, William Blumenthal, *Why Bother?: Or Market Definitions Under the Merger Guidelines*, Statement before the FTC/DOJ Merger Workshop (Feb. 17, 2004), available at http://www.ftc.gov/bc/mergerenforce/presentations/040217blumenthal.pdf.

27 *See, e.g.*, *Royal Caribbean Cruises*, *supra*.

28 *Merger Guidelines*, §1.5.

29 *United States v. Baker Hughes, Inc.*, 908 F. 2d 981 (D.C. Cir.1990). Prior to *Baker Hughes*, the Division placed extraordinary weight on market concentration in litigation, focusing much less on other factors evidencing competition.

30 *Arch Coal*, at 145-46; *Oracle*, at 1110-12.

B. Competitive Effects

The *Merger Guidelines* approach to coordinated effects has been criticized by some as an unstructural "checklist" and as being "too crude to provide much assistance in determining whether a coordinated interaction theory is relevant" because, among other concerns, "many industries that fit the checklist do not appear to exhibit outcomes that are consistent with coordinated interaction.[31]

The market conditions listed as those conducive to coordinated interaction should not be viewed as a checklist, but rather as a starting point for the analysis of the competitive effects of a transaction. No priority is given to one element over another, and this was intentional. The importance of any one factor will vary significantly depending on the facts and circumstances of any given case. The *Merger Guidelines* are flexible enough to offer guidance for merger review across all industries. Indeed, among other goals, the *Merger Guidelines* were designed to offer some predictability regarding the review process and the types of evidence that will be considered in a merger investigation.

Nonetheless, efforts to build on the foundation provided by the *Merger Guidelines* are ongoing and need to continue. Merger investigations, case decisions, economic studies and public statements by DOJ and FTC officials all provide insight into what factors are most important under different circumstances.

1. Customer Testimony

Progress is steadily being made toward a refinement of the types of customer evidence that "matter" in merger analysis. For example, recent court decisions have provided insight into the proper weight that should be afforded to customer testimony.

Customer reaction to a proposed transaction has traditionally been regarded as a very important factor in evaluating probable competitive effects, but the recent *Arch Coal* and *Oracle* decisions criticized the government for failing to provide customer testimony based on "hard

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[31] Scheffman and Coleman, *supra.*

evidence" or supported by well-informed experience.[32] In these cases, the courts concluded that the customer testimony was not persuasive because it was limited to general fears of reduced competition,[33] or because it amounted to no more than expressions of strong customer preferences.[34] In both cases, it seems that the courts implicitly criticized the customer testimony for failing to address the specified types of information identified in the *Merger Guidelines*.

The court's implicit criticism of customer testimony in *Arch Coal* was that it did not address the market conditions conducive to coordinated interaction that are identified in the *Merger Guidelines*.[35] Rather, customers merely expressed concern that a reduction in the number of bidders might lead to reduced competition.

> "[W]hile the Court does not doubt the sincerity of the anxiety expressed by . . . customers, the substance of the concern articulated by the customers is little more than a truism of economics; a decrease in the number of suppliers may lead to a decrease in the level of competition in the market. Customers do not, of course, have the expertise to state what will happen . . . in the market, and none have attempted to do so."[36]

Similarly in *Oracle* the court discounted much of the government's customer testimony because it failed to offer hard evidence that addressed the market definition test identified in the *Merger Guidelines*. The testimony did not offer convincing evidence that customers could not substitute other suppliers' products for those supplied by the merging parties. Customers testified that they preferred the merging parties' products, but their testimony failed to seriously address the key issue of interchangeability.

> "Customer preferences towards one product over another do not negate interchangeability . . .[T]he issue is not what solutions the customers would *like* or *prefer* for their data processing needs; the issue is

[32] *Arch Coal,* at 145-46; *Oracle,* at 1131.

[33] *Arch Coal, supra.*

[34] *Oracle, supra.*

[35] *Arch Coal, supra.*

[36] *Id.*

> what they *could* do in the event of an anticompetitive price increase by a post-merger Oracle. Although these witnesses speculated on that subject, their speculation was not backed up by serious analysis that they had themselves performed or evidence they presented . . . If backed by credible and convincing testimony of this kind or testimony presented by economic experts, customer testimony of the kind plaintiffs offered can put a human perspective or face on the injury to competition that plaintiffs allege. But unsubstantiated customer apprehensions do not substitute for hard evidence."[37]

The agencies appropriately continue to rate customer testimony as an important element in merger review.[38] Recent court decisions have led the agencies to drill deeply into customer views to ascertain their foundation, including their timely experience with industry participants, relationships with vendors, and relevant planning materials.

2. Buyer Power

Another example of the ongoing efforts to refine and add depth to the factors identified in the *Merger Guidelines* is the body of knowledge that has been developed in connection with the "power-buyer" defense. The *Merger Guidelines* identify buyer power, or more precisely, "buyer characteristics and the nature of the procurement process" as one factor that must be considered in analyzing a merger's potential to facilitate coordinated interaction.[39] In a number of close cases, the presence of powerful buyers was an important factor in determining that a merger with high market shares was nevertheless unlikely to cause harmful post-merger competitive effects.[40]

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[37] *Oracle, supra.*

[38] See Deborah Platt Majoras, Chairman, Federal Trade Commission, *Looking Forward: Merger and Other Policy Initiatives at the FTC*, Remarks before the American Bar Association Antitrust Section Fall Forum, Washington, D.C., November 18, 2004, available at http://www.ftc.gov/speeches/majoras/041118abafallforum.pdf; Deborah Platt Majoras, Chairman, Federal Trade Commission, *Recent Developments at the FTC*, remarks before the Dallas Bar Association's Section on Antitrust and Trade Regulation, Dallas, TX, January 18, 2005, available at http://www.ftc.gov/speeches/majoras/050126recentactions.pdf.

[39] *Merger Guidelines,* § 2.12.

[40] *See United States v. Archer Daniels-Midland Co.*, 1991-2 Trade Case (CCH) ¶ 69,647 (S.D. Iowa 1991) (The court identified numerous specific tactics that buyers had used to discipline suppliers including "playing suppliers against one another, swinging volume back and forth among suppliers, disciplining sellers by cutting them off entirely, successfully insisting on year long or multi-year tolling agreements, and holding out the threat of inducing a new entrant . . ."); *see also United States v. Baker Hughes, Inc.*, 908 F. 2d 981, 982 (D.C. Cir. 1990); *United States v. Syufy Enterprises*, 903 F. 2d 659 (9th Cir. 1990); *United States v. Country Lake Foods*, 754 F. Supp. 669, 675 (D.

As a result of these decisions, the enforcement agencies have elaborated on the circumstances under which power buyers are, or are not, likely to constrain anticompetitive behavior.[41] It is now well established that the proposition requires more than evidence that customers are large and sophisticated. In order to constrain anticompetitive behavior such buyers must also have access to reasonable commercial alternatives. The structure of market demand is also important. Customers' alternative suppliers, which may consist of a fringe of smaller suppliers or potential entrants, must have sufficient capacity and/or the ability to expand to meet the new demand quickly.[42] A buyer can only discipline the merging parties by shifting purchases to smaller fringe players, or new entrants, if the new suppliers have enough surplus capacity to satisfy the orders.[43]

Aside from instances where customers might lack viable alternatives, enforcement officials have identified numerous additional circumstances that would undermine the effectiveness of power-buyers. For example, complex products with a large number of inputs may make it difficult for buyers to recognize anticompetitive price increases. Reputation and reliability factors may inhibit the rapid switching of suppliers. The need for business flexibility

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Minn. 1990); *FTC v. R.R. Donnelly & Sons*, 1990-2 Trade Case. (CCH) ¶ 69,239 (D.D.C. 1990). Some question has been raised regarding the accuracy of the *ADM* court's perception of power buyers' ability to prevent coordination in the context of a proximate market. Deputy Assistant Attorney General William Kolasky has noted that both the victims and the acquiring party were involved in the subsequent citric acid cartel case. W. J. Kolasky, *Coordinated Effects in Merger Review: From Dead Frenchmen to Beautiful Minds and Mavericks*, remarks before the ABA Section of Antitrust Spring Meeting, Washington, D.C. (April 24, 2002).

41 Mary Lou Steptoe, Deputy Director FTC Bureau of Competition, *The Power Buyer Defense in Merger Cases,* Remarks before the American Bar Association Section of Antitrust Law (Aug. 10, 1992).

42 "In its analysis of the 2005 acquisition of Varco, Inc. by National Oilwell Inc., the DOJ found that large customers would effectively sponsor entry by committing to purchase from other companies that would expand their product lines or production capacity. Organization for Economic Co-operation and Development, Directorate for Financial and Enterprise Affairs Competition Committee, Roundtable on Barriers to Entry, Note by the United States ¶ 20, (October 2005).

43 *See* Steptoe, Remarks Before the American Bar Association, at 11.

may prohibit the use of large volume or long-term contracts. And, barriers may prohibit power buyers from inducing entry.[44]

3. Fringe Expansion

"Maverick" language can be taken to focus on removal of mavericks through merger as evidence of anticompetitive effect. The *Merger Guidelines* also indicate that the post-merger presence of a maverick, party or nonparty, would indicate the merger does not threaten competition and may even be pro-competitive. Thus, the *Merger Guidelines* indicate that a fringe player might frustrate coordination by having greater incentive to deviate from coordination and focus on the divertible capacity of non-merging firms in relation to their sales and the cost, including opportunity costs of diversion.[45] As observed by Jonathan Baker, ". . . the concept of a maverick can operate as a sword or a shield in merger review, helping distinguish anticompetitive mergers from procompetitive ones."[46]

4. Unilateral Effects

It has been argued that the *Oracle* decision may call for "serious revision" of the unilateral effects provisions of the *Merger Guidelines*,[47] but the unilateral effects approach is sufficiently broad to accommodate development in economic learning and to comprehend rich and complex fact situations.

The criticism that these guidelines provisions rest inordinately on narrow market share presumptions fails to come to grips with the full context of the unilateral effects section. Although the *Merger Guidelines* provide that one test for the competitive proximity of the

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44 *Id.*

45 *Merger Guidelines*, § 2.12, n. 3.

46 Jonathan B. Baker, *Mavericks, Mergers and Exclusion* at 177. *See*, *Cardinal Health*, 12 F. Supp. 2d 34, 63-64. (D.D.C. 1998) (available capacity leads to maverick behavior).

47 *See, e.g.*, James A. Keyte, *Arch and Oracle Put the Agencies on the Ropes in Proving Anticompetitive Effects*, 18 ANTITRUST 79, 85 (Fall 2004).

products of the merging firms,[48] that approach is qualified by footnote 22, requiring empirical information of customer choice, and recognition that market shares may either understate or overstate the competitive nexus.[49]

The district court in *Oracle*, while critical of the *Merger Guidelines*' market-share language, acknowledged that the discussion "may be a helpful start" and, more importantly, pointed to the further condition of the *Merger Guidelines* that other firms not be capable of repositioning such that any putative unilateral effect of a merger[50] would be dissipated. [51]

Judge Walker in *Oracle* extolled the "promise" of economic simulation in unilateral effects analysis[52] but found that the government did not uphold its burden in presenting such evidence nor did it provide adequate qualitative evidence to sustain its designated product market. The court did carefully evaluate evidence presented by customers, actual and potential, and experts in reaching its conclusion. Similarly, in *Swedish Match*,[53] the court, while evaluating econometric evidence, rested its market definition conclusion on empirical proof of actual market circumstances. Thus, while econometric simulation has "promise", in the words of Judge Walker, it has not yet achieved the primetime rating so as to be decisive in any case. *Oracle* and *Swedish Match* as well as the plethora of economic commentary do, nevertheless,

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[48] *Merger Guidelines*, §2.21.

[49] Some critics suggest that relative market shares tell nothing about the relative importance of the sellers products as direct competitors. *See*, Gregory J. Werden & George A. Rozanski, *The Application of Section 7 to Differentiated Products Industries*, 8 Antitrust 40, 41 (Summer 1994).

[50] The *Oracle* court also rejected the 35 percent threshold ("presumption") the guidelines, holding that a plaintiff claiming unlawful unilateral effects of a merger must demonstrate that the parties would achieve a dominant position. *Oracle*, at 1123. The 35 percent threshold is designed as a limitation, albeit an imperfect one, on the inference of product proximity that might otherwise be drawn from relative market shares. As such, it has been criticized as creating the risk of type two, not type one, error. *See* DOJ-FTC Joint Workshop on Merger Enforcement, Day 3 (Feb. 19, 2004), comments of Jonathan B. Baker at 137-138.

[51] *Oracle*, at 1116-17.

[52] *Oracle*, at 1122-23.

[53] *Swedish Match*, at 162-165.

strongly encourage more intensive work with the methodology and, equally important, have increased efforts to make it more coordinated with qualitative empirical evidence such as firm documents, informal customer statements, and natural experiments, and more transparent to courts and parties.

There is nothing in the unilateral effects section or elsewhere in the *Merger Guidelines* that precludes reliance on such analysis where it is credible, technically sound, and compelling. The *Merger Guidelines* application depends on the extent to which the products of the merging firms are in immediate proximity and the capacity for repositioning by other firms in the market. They suggest, but do not prescribe, the avenues by which these conclusions might accurately be reached.

C. Efficiencies

In view of the fact that another panel will be considering efficiencies in detail, a few brief comments will suffice in this paper.

The *Merger Guidelines* do not preclude recognition of longer-term cost savings that are demonstrable and merger specific. This principle was expressed in the 1997 revision to the *Merger Guidelines,* which undertook to provide further guidance regarding the approach to efficiencies in merger review. Footnote 37 to the *Merger Guidelines* provides that the agencies will consider cognizable efficiencies that do not have a short-term price effect although accord them less weight as being less capable of sure verification.[54]

The FTC Staff Report, *Anticipating the 21st Century: Competition Policy in the New High-Tech Global Marketplace*, provides historical context for the 1997 amendments in including, ". . . an arbitrary exclusion of fixed costs from cognizable efficiencies is unwarranted because savings in fixed costs may affect competition and have an ultimate downward effect on price."[55] Similarly, the FTC Staff Report provides the groundwork for the recognition of

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[54] *Merger Guidelines*, § 4, n. 37.

[55] FTC Staff Report, *Anticipating the 21st Century Competition Policy in the New High-Tech Global Marketplace*, Ex. 132, p. 34, available at http://www.ftc.gov/opp/global/report/gc_v2.pdf.

dynamic efficiencies in explaining that the efficiencies have the capacity to "affect the merged firm's abilities and incentives to compete" and thereby "improve the competitive performance of the market(s) in which the merger firm operates . . .".[56]

The *Merger Guidelines*, as revised, also make clear the requirement that efficiencies be merger specific does not mandate comparison with a "merely theoretical" less restrictive alternative.[57] Commenting on the revision, former-Chairman Muris explained, "[T]he focus should not be on whether another method might exist to lower costs, but instead on whether the method is more or less costly than the merger and whether it can be implemented as rapidly as the merger."[58] The revised *Merger Guidelines* are amenable to this approach.

Recent district court decisions rejecting the efficiency claims of the parties have done so on evidentiary shortcomings regarding merger specificity[59] or verifiability.[60] These decisions do not signal any unduly narrow scope of the *Merger Guidelines*. Noteworthy in this regard is the recent Department of Justice statement in settlement of the Verizon-MCI and SBC-AT&T mergers, where a broad range of savings are described as showing "exceptionally large merger-specific efficiencies."[61]

The Court of Appeals in *Heinz* did adopt the "sliding-scale"[62] concept, advanced in the *Merger Guidelines*, whereby the proof of certainty and magnitude of efficiencies is increased as the degree of potential for competitive harm increases. This concept has been questioned since

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56 *Id*, p. 24-25.

57 *Merger Guidelines*, § 4.

58 Timothy J. Muris, *The Government and Merger Efficiencies: Still Hostile After All These Years*, 7 GEO. MASON L. REV. 729, 732 (1999).

59 *Arch Coal*, at 150-153.

60 *Oracle, supra*.

61 *See*, U.S. Dept. of Justice press release dated October 27, 2005, "Justice Department Requires Divestitures Verizon's Acquisition of MCI and SBC's Acquisition of AT&T".

62 *Heinz*, at 720-722.

the issuance of the 1992 *Merger Guidelines*. Nevertheless, the court went further to reject the parties' efficiencies claims on grounds of both merger specificity and verifiability.

IV. CONCLUSION

The agencies should continue to provide guidance, in the form of transparent consents and closing letters, studies, workshops, and speeches, regarding the application of the *Merger Guidelines*, but there is no need at this time to reopen the *Merger Guidelines*. In their current form, the *Merger Guidelines* provide appropriate guidance to lawyers and businesses, while retaining sufficient flexibility to apply to new and evolving fact patterns. Premature efforts to "codify" the antitrust treatment of issues as to which the analysis is continuing to incubate in the agencies, academia, and the courts should be avoided.