Editor's Note: Enforcement Changes: Evolution or Revolution?

BY DEBORAH L. FEINSTEIN

ANY TIME A NEW GROUP OF antitrust enforcers comes into office, there is considerable speculation about their effect on enforcement activities. When Tim Muris became Chairman of the Federal Trade Commission in 2001, he sought to allay concerns that dramatic changes would take place.[1] In contrast, the current enforcement heads have not sought to quell speculation about change.

Nowhere is the change in enforcers more likely to be evident than in the merger area. The agencies have solicited public comment on a series of questions[2] and announced workshops to explore a possible update to the Merger Guidelines. The stated goal is "to determine whether the Horizontal Merger Guidelines accurately reflect the current practice of merger review at the Department and the FTC as well as to take into account legal and economic developments that have occurred since the last significant Guidelines revision in 1992."[3]

Whether to change the Merger Guidelines and how to change them are not easy issues. Our Roundtable Discussion in this issue pointed to general consensus that certain aspects of the Guidelines do not reflect actual agency practice and may warrant reform, specifically:

- The HHIs thresholds and presumptions are not reflected in the actual cases the agencies bring;
- The 35 percent presumption in the unilateral effects section is confusing; and
- The distinction between committed and uncommitted entry is not well understood or applied.

Yet there is, unsurprisingly, some anxiety about how the Merger Guidelines might change—not only about how changes would affect merger challenges, but also how changes would affect the ability of practitioners to advise their clients accurately. The enforcers have taken an important first step in soliciting views on these issues. I offer a few of my own.

Consider the purpose of the Guidelines: One of the major criticisms of the current Guidelines is that they do not reflect actual agency practice. Implicit in that comment is that the purpose of the Guidelines is to set forth the agencies' enforcement intent—and perhaps to guide staff. Of course, there is also another potential purpose of the Guidelines—to help guide the courts on the agencies' views as to the proper way to analyze mergers. At times, these purposes can be in tension. The bright line rules and presumptions the agencies may find helpful in court, and that can provide some guidance to parties contemplating a merger—may not actually reflect the nuanced manner in which the agencies actually conduct a merger review. A careful balancing of these competing considerations will be necessary to have a useful and meaningful document.

Consider what worked well in the 1992 Merger Guidelines: One of the most noteworthy aspects of the 1992 Merger Guidelines is how long they have endured. There is no doubt that they have begun to fray around the edges. The Merger Commentary was an effort to update the agencies' guidance with respect to how it conducted merger analysis without actually revising the Guidelines. Nevertheless, the basic framework and mode of analysis has endured. And while certain of the revisions seemed revolutionary—or at least evolutionary—at the time, it did not take long for concepts like "close substitutes" and "timely, likely and sufficient" to become part of the everyday language with which practitioners were at least relatively comfortable conversing and advising. That is not to say that the 1992 Guidelines avoided ambiguity or controversy. But for the most part, the Guidelines helped practitioners advise their clients on all but the closest of cases.

Consider what did not work well in the 1992 Merger Guidelines: Among the major criticisms of the 1992 Guidelines are the efforts to create bright lines and hold on to some of the presumptions of the past. The HHI thresholds—almost from the start—were lower than anyone thought would likely lead to enforcement actions. The Guidelines statement that, in certain circumstances in which the merging companies' combined share was 35 percent, "the Agency would presume that a significant share of sales in the market are accounted for by consumers who regard the products of the merging firms as their first and second choices"[4] was poorly understood and untethered to any economic basis. Further, it is unclear to what extent it was really used—other than in court. Before instituting a new set of presumptions, the agencies should tread cautiously.

Base them on experience: One question the agencies ask is whether the Guidelines should address more explicitly "the non-price effects of mergers, especially the effects of mergers on innovation." While the agencies, particularly the FTC in pharmaceutical cases, have brought enforcement actions based on a theory of a reduction in innovation, they have never put forth guidelines on the subject. There is every reason to question whether they should do so now. The literature is at best mixed on the question of whether a reduction in the number of research "competitors" can be presumed to adversely affect the likelihood of innovation.[5] Before the agencies issue guidelines on this subject, they should undertake a serious examination of

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whether transactions that combine two innovators in fact harms consumers. Did the would-be merging parties bring to market products in a reasonable period of time? Were they ahead of other competitors in doing so? Much was made in the Ciba/-Sandoz case of the need to require a licensing remedy since Ciba and Sandoz "are two of only a few" entities capable of commercially developing gene therapy products.[6] Yet twelve years later there are no gene therapy products on the market. In retrospect, there would seem to have been no likelihood of anticompetitive effects from that transaction to justify a remedy.

Make them practical: One benefit of the 1992 Guidelines presumptions based on HHIs is that applying the initial HHI screen was fairly easy. Obtaining market shares—even if for a range of possible markets—is something business people often do in the ordinary course of business. While the market definition and competitive effects analysis might pose issues, one could at least say "If the market is x, it is highly concentrated and problematic. If it is y, the transaction will be cleared. So let's dig harder to figure out how the government might define the market." Some have speculated, however, that the upward pricing pressure (UPP) model, as described by Carl Shapiro and Joe Farrell, respectively the chief economists at the DOJ and the FTC, might replace the HHIs as the new screen. Even assuming the UPP model might be appropriate in some markets, it seems very difficult for parties to figure out how to apply it as an initial screen. In many industries, diversion ratios are not readily accessible, nor are they easy to estimate. The proper calculation of margins can be difficult. Unlike HHI analysis, which can often be done with business people in an hour or two, applying the UPP model would appear to be significantly harder, making it much more difficult to provide basic guidance on the outcome of a transaction without undertaking an extensive economic exercise.

Consider the relationship between substantive analysis and the review process: Substantive analysis cannot be divorced entirely from the realities of the review process. The use of electronic documents has greatly increased the availability of documents and data that can be used in a merger analysis. More sophisticated economic tools require more extensive amounts of data. The combination of the two has led to a situation where complying with a Second Request has become increasingly unwieldy, burdensome, and expensive. It would be unfortunate if the Merger Guidelines substantive analysis inevitably required extensive amounts of data and documents to be analyzed in a much greater number of transactions.

Consider the need for greater transparency: One of the purposes of the Merger Guidelines is to advise parties on the analysis the agencies will undertake in considering whether to take enforcement action against a particular transaction. But the transparency should not stop there. Parties have a right to know how the Guidelines are being applied to their transaction, what the agencies are grappling with, what facts and information they believe are useful, and, perhaps most importantly, what economic analysis is relevant. Too many times, parties spend millions of dollars undertaking economic analysis to have the agency staff simply respond by saying it is not convincing—with no explanation as to whether it addresses the wrong theory, uses incorrect models, is based on flawed assumptions, or uses incorrect data. Transparency during the investigation is not only a matter of fundamental fairness, but the ensuing dialogue will lead to better results and a greater understanding of how the Merger Guidelines should be applied in practice.

The transparency should not end there. Closing statements are an extremely important way for those on the outside to understand how the agencies are conducting merger analysis. The recent Pfizer/Wyeth statement is as interesting for what it says the FTC considered as it is for the enforcement action it took. While explaining the rationale for requiring a remedy in the animal health area, the Commission also assessed "whether a combined Pfizer/Wyeth would have a greater ability to engage in anticompetitive bundling, block new drug development with a merger-created patent thicket, or adversely impact the market for basic research and innovation in any human health markets."[7] These issues appear to go beyond the traditional horizontal and innovation theories the FTC typically analyzes and put practitioners on notice that such issues could arise in other transactions as well.

Don't let perfect be the enemy of good: The desire to write Guidelines that are analytically sound, easy to administer, practical, and understandable is a laudable and important goal. But it will not be easy. Lawyers and economists across two agencies will have to agree on a single guiding document, and compromise is inevitable. If the way the agencies analyze transactions has changed—and is expected to change further—taking two years to write Guidelines (the time it took to write the 1992 Guidelines) is too long to inform outside parties and practitioners of changes in enforcement intent. The "perfect" Guidelines are unattainable; but Guidelines that aim high and come close to the mark will be welcomed. ■

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1 Timothy J. Muris, Chairman, Federal Trade Commission, Prepared Remarks Before ABA Section of Antitrust Law Annual Meeting (Aug. 7, 2001).

2 Fed. Trade Comm'n & U.S. Dep't of Justice, Horizontal Merger Guidelines: Questions for Public Comment (Sept. 22, 2009), *available at* http://www.ftc.gov/bc/workshops/hmg/hmg-questons.pdf.

3 Federal Trade Commission and Department of Justice to Hold Workshops Concerning Horizontal Merger Guidelines: Antitrust Agencies Explore Possible Update to Guidelines to Account for Legal and Economic Developments (Sept. 22, 2009), http://www2.ftc.gov/opa/2009/09/mgr.shtm.

4 U.S. Dep't of Justice and Fed. Trade Comm'n Horizontal Merger Guidelines (1992, revised 1997), *available at* http://www.ftc.gov/bc/docs/horizmer.shtm.

5 *See* Dennis W. Carlton & Robert H. Gertner, *Intellectual Property, Antitrust and Strategic Behavior*, *in* 3 INNOVATION POLICY AND THE ECONOMY (NBER, Adam B. Joffee, Josh Lerner & Scott Stern eds., 2003).

6 Ciba-Geigy, FTC Docket No. C-3725 (Mar. 24, 1997), *available at* http://www.ftc.gov/os/1997/04/c3725cmp.pdf.

7 Statement of the Federal Trade Commission Concerning Pfizer/Wyeth, FTC File No. 091-0053 (Oct. 14, 2009), *available at* http://www.ftc.gov/os/caselist/0910053/091014pwyethstmt.pdf.