

1001 G Street, N.W.  
Suite 500 West  
Washington, D.C. 20001  
tel. 202.434.4100  
fax 202.434.4646

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**Writer's Direct Access**  
**Peter L. de la Cruz**  
(202) 434-4141  
delacruz@khlaw.com

HMG Review Project - Comment  
Project No. P092900  
Federal Trade Commission  
Room H-135 (Annex P)  
600 Pennsylvania Avenue, N.W.  
Washington, D.C. 20580

**Re: Horizontal Merger Guidelines**

Dear FTC/DOJ Merger Guidelines Working Group Members:

Because it has not been discussed in other comments, this letter addresses the market definition sections of the Horizontal Merger Guidelines<sup>1</sup> when mergers involve multi-tiered markets or markets in which the merging parties may have both upstream and downstream market power. The current guidelines do not directly address this issue and it would be prudent for the revisions to reference this scenario and provide guidance for parties considering and evaluating merger transactions.

The Market Definition, Measurement and Concentration sections of the current Horizontal Merger Guidelines leave the reader with the impression that the market definition exercise is confined to narrow markets in which the assessment concerns only the roles of the merging parties as sellers and their ability to impose price increases on buyers. While efforts are made "to define a market in which firms could effectively exercise market power, if they are able to coordinate their actions" (Section 1.0 - Overview), the market definition process, as described, is focused on coordination with respect to sales of the product manufactured by the firms at issue. Notably, the Guidelines narrow the focus with the notion that:

[a] market is defined as a product or group of products and a geographic area in which it is produced or sold such that a hypothetical profit-maximizing firm, not subject to price regulation, that was the only present and future producer or seller of those products in that area likely would impose at least a 'small

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<sup>1</sup> U.S. Department of Justice and the Federal Trade Commission, "Horizontal Merger Guidelines" (April 1992), as amended April 1997.

but significant, nontransitory' increase in price, assuming the terms of sale of all other products are held constant.<sup>2</sup>

This same premise is repeated in Section 1.11 on Product Market Definition, which states that the agencies "will delineate the product market to be a product or group of products such that a hypothetical profit-maximizing firm that was the only present and future seller of those products ("monopolists") likely would impose at least a 'small but significant and non-transitory' increase in price." The additional element identified in that section with respect to the assessment of the product market definition is "the likely reaction of buyers to a price increase." The geographic market definition approach, as set forth in Section 1.2 of the Guidelines, is likewise tailored, in most respects, on this narrow description of the product market definition exercise.

The narrow approach to the product and geographic market definition exercise set forth in the Guidelines appears to be at odds with the approach taken by the agencies in a number of circumstances as well as the approaches adopted and utilized by other competition authorities including the Australian Competition and Consumer Commission<sup>3</sup> ("ACCC") and the European Commission<sup>4</sup> ("EC"), as well as principles laid out in the International Competition Network Merger Guidelines Workbook.<sup>5</sup>

In terms of the U.S. approach to market definition with respect to multi-tiered upstream and downstream markets, the product market definition exercise undertaken by U.S. agencies has been broadened to include such markets in a number of instances. While three of those cases are mentioned in this brief commentary, a comprehensive review was not undertaken to identify each and every instance in which such an approach was adopted. Each of these merger reviews, however, highlights the importance of, and the need for, further clarity in the Merger Guidelines concerning potential use of broader approaches to product and geographic market definition.

In the Department of Justice's review of Aetna, Inc.'s proposed acquisition of certain health insurance-related assets of The Prudential Insurance Company of America, the

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<sup>2</sup> *Id.* at 1, 1.0

<sup>3</sup> *Merger Guidelines*, Australian Competition and Consumer Commission, 15-23 (Nov. 2008), available at <http://www.accc.gov.au/content/item.phtml?itemId=809866&nodeId=7cfe08f3df2fe6090df7b6239c47d063&fn=Merger%20guidelines%202008.pdf>.

<sup>4</sup> *Commission Notice on the Definition of Relevant Market for the Purposes of Community Competition Law*, Official Journal of the European Union, C372/3, 5-13 (Sept. 12, 1997), available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:31997Y1209%2801%29:EN:HTML>.

<sup>5</sup> *ICN Merger Guidelines Workbook*, ICN Merger Working Group, Investigation and Analysis Subgroup, 15-30 (April 2006), available at [http://www.reseauinternationaldelaconcurrence.org/media/library/conference\\_5th\\_capetown\\_2006/ICNMergerGuidelinesWorkbook.pdf](http://www.reseauinternationaldelaconcurrence.org/media/library/conference_5th_capetown_2006/ICNMergerGuidelinesWorkbook.pdf).

Department of Justice expressed concern in its complaint that the acquisition would not only increase prices consumers paid for certain health insurance coverage, but would also increase the combined firm's buyer power and enable Aetna to reduce physician reimbursement rates.<sup>6</sup> In assessing Aetna's buyer power and the appropriate product market definition, the Department of Justice noted, among other things, that Aetna would account for a large share of all payments to physicians in the Houston and Dallas area and that the combined firm's ability to depress physician reimbursement rates would likely lead to a reduction in quantity or degradation in quality of physician services.<sup>7</sup> In that situation, the Department of Justice clearly recognized that it needed to consider, in the product market definition exercise, not only the downstream consumer impact with respect to how much consumers paid for health insurance coverage, but also the upstream impact on suppliers (here physicians) of the enhanced purchasing power of the combined entities. In analyzing the enhanced purchasing power of the combined entities as part of the product market definition exercise, the Department of Justice considered whether the physicians had "good" alternative buyers for their services and the impact that "[a] small but significant decrease in the prices paid" would have on the physicians' conduct and profitability.<sup>8</sup> In essence, the same SSNIP test was utilized but with respect to buying/supply, as opposed to sale, market.

Likewise, in *In re Shell Oil Co.*,<sup>9</sup> the Federal Trade Commission (FTC) challenged the formation by Shell and Texaco of the joint venture that was ultimately the subject of the private litigation resulting in the Supreme Court's decision, *Texaco Inc. v. Dagher*.<sup>10</sup> Although the proposed joint venture only combined the companies' upstream (refining, transportation and marketing) operations, the FTC also analyzed the competitive effects of the joint venture in the downstream (wholesale and retail sales) markets. As such, the FTC defined the relevant product markets to include not only the refining, transportation and terminaling of gasoline markets, but also the downstream wholesale and retail sales of gasoline and related petrochemical products.

Similarly, in the Department of Justice's challenge to the consummated acquisition of the Northwest Arkansas Times by interests owning the competing Morning News of Northwest Arkansas, multi-tiered markets were defined and identified.<sup>11</sup> There, the Department of Justice

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<sup>6</sup> *United States v. Aetna, Inc.*, No. 3-99 CV 398-H, Pl's. Comp. at 2 (N.D. Tex. June 21, 1999), available at <http://www.justice.gov/atr/cases/f2500/2501.pdf>.

<sup>7</sup> See *id.* at 10-11.

<sup>8</sup> See *id.* at 8-9.

<sup>9</sup> *In re Shell Oil Co.*, Dkt. No. C-3803 (F.T.C. Apr. 21, 1998), available at <http://www.ftc.gov/os/1998/04/9710026.cmp.htm>.

<sup>10</sup> *Texaco Inc. v. Dagher*, 547 U.S. 1 (2006).

<sup>11</sup> *United States v. NAT, L.C.*, No. 95-5048 (Mar. 28, 1995).

asserted that the merger would likely harm the downstream market of consumers (subscribers of the newspapers) as well as the upstream advertising market.

The approach reflected in these three cases recognized multi-tiered markets and the need to look at both upstream and downstream markets in the market definition exercise, and the potential impact of both buyer and seller power. These conditions are not unique to these cases or to the United States. This approach is widely accepted. In the ICN Merger Guidelines Workbook's discussion of product market definition, the Woolworth's/ Foodland Associated Limited competition assessment by the ACCC is featured as a case study.<sup>12</sup> In that assessment, the ACCC considered the proposed acquisition of grocery stores and development sites by a competing supermarket operator. In their competition assessment, the ACCC discussed market definition, noting that it "adopts a purposive approach in defining the relevant markets, focusing on defining the relevant market(s) in the context of the specific proposal before it."<sup>13</sup> Utilizing that definitional approach, the ACCC identified three markets. First, in line with the "SSNIP" test, they identified the local supermarket market in which grocers compete to provide goods and services to consumers within a limited geographic area.<sup>14</sup> The ACCC also identified two upstream markets for the supply of grocery products. The first market, described as the "procurement market," focused on the upstream regional market for the supply of fresh products to supermarkets.<sup>15</sup> The second upstream market identified was the "national wholesale market" for the supply and distribution of goods to supermarkets for retail sale.<sup>16</sup>

The approach adopted by the ACCC in Woolworth's/Foodland is similar to the approach utilized by the EC and EU member states. For example, the approach utilized by the EC in the definition of markets in its evaluation of the *Kesko/Tuko*<sup>17</sup> merger led to the identification of a downstream market for sales to consumers as well as upstream supply markets for the procurement of goods by the retailers at issue. In that context, the EC recognized that, in the upstream supply market, the retailers performed a "gatekeeper" function. Thus, there was a need

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<sup>12</sup> *ICN Merger Guidelines Workbook* at 89.

<sup>13</sup> *Woolworths' Proposed Acquisition of 22 Action Stores and Development Sites*, ACCC Public Competition Assessment, 3 (Oct. 19, 2005) available at <http://www.accc.gov.au/content/trimFile.phtml?trimFileName=D05+63026.pdf&trimFileTitle=D05+63026.pdf&trimFileFromVersionId=711311>.

<sup>14</sup> *See id.* at 5.

<sup>15</sup> *Id.*

<sup>16</sup> *Id.*

<sup>17</sup> Case No. IV/M. 784 - *Kesko/Tuko*, decision of November 20, 1996, reported in the Official Journal of the European Communities (ECJ), No. L 110/53, April 26, 1997.

to separately define and evaluate the likely effects of the merger in the context of that market and the retailers' gatekeeper function and buyer power.

The notion that multiple markets may be at issue in a particular merger is not novel. It has been recognized by the U.S. agencies, in, among others, the merger situations discussed above. Indeed, the approach recommended here is consistent with agencies' prior pledge to "examine all plausible markets to determine whether an adverse competitive effect is likely to occur in any of them."<sup>18</sup> It is also a standard and accepted approach among other prominent competition authorities. Given the broader perspective on market definition that is embodied both by the actual practices of the U.S. agencies and by these accepted approaches to market definition, it would be prudent to include a broader discussion in the Horizontal Merger Guidelines concerning the circumstances in which the U.S. agencies will take a broader approach to market definition than the more narrow downstream and "SSNIP" test focused approach outlined in the guidelines, and how the agencies will undertake to define markets when presented with situations with multi-tiered markets and upstream and downstream competitive effects. At a minimum, the Guidelines should include an explicit statement that the agencies will evaluate competitive effects in all potentially relevant markets, including upstream and downstream effects. The provision of this guidance will make the Guidelines a more complete document and will provide for more robust understanding and direction for the benefit of the agencies, and the commercial and legal community who rely upon the Guidelines for merger review and evaluation.

I appreciate the opportunity to provide this commentary. To the extent that I may be able to provide further assistance or guidance with respect to the implementation of proposed changes, as outlined herein, please do let me know.

Sincerely,

Peter L. de la Cruz

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<sup>18</sup> FTC/DOJ, "Commentary on the Horizontal Merger Guidelines," 5 (Mar. 2006). *See also, id.* at 12: "The process of defining the relevant market is directly linked to competitive effects analysis. In analyzing mergers, the Agencies identify specific risks of potential anticompetitive harm, and delineate the appropriate markets within which to evaluate the likelihood of such potential harm."

KELLER AND HECKMAN LLP

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cc: Assistant Attorney General Christine Varney  
950 Pennsylvania Ave., N.W.  
Washington, D.C. 20580

Chairman Jon Leibowitz  
Federal Trade Commission  
600 Pennsylvania Avenue, N.W.  
Washington, D.C. 20580