Federal Trade Commission

NAVIGATING THE MERGER WATERS AT THE FEDERAL TRADE COMMISSION: WHAT MATTERS

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I. Introduction[1]

Merger enforcement is a core component of the Federal Trade Commission ("FTC" or "Commission") mission to preserve competition and promote innovation, while ensuring that consumers benefit from efficient mergers. Since 2006, the Commission has brought enforcement actions in over thirty mergers. In several instances, the parties abandoned their transactions after being alerted to staff's concerns regarding the legality of their merger. In other cases, the Commission was able to maintain or restore competition in a particular relevant market by allowing the parties to consummate their merger subject to an order requiring divestiture of assets to a third party. During the same period of time, the Commission also litigated three preliminary injunction actions in federal district court seeking to block proposed merger transactions in which the Commission had reason to believe that the merger would be anticompetitive.

This presentation will be divided into two parts. The first part will highlight recent enforcement activity at the FTC. I will review some of the recent transactions in which the Commission obtained structural relief in the form of divestitures to eliminate harm. I will also briefly review the FTC's recent court challenges in the Whole Foods/Wild Oats, Equitable/Dominion, and Western Refining/Giant Industries transactions. The second part of this presentation will discuss improvements to the merger review process. Such improvements include reforms to the requests for additional information and documentary material ("second

[1]The views expressed in this presentation are my own and not those of the Federal Trade Commission or any individual Commissioner.

requests") issued by the FTC in 2006[2], as well as increased transparency of the FTC and Department of Justice Antitrust Division ("DOJ" or "Antitrust Division") decision-making process through joint issuance of a commentary on the Horizontal Merger Guidelines.[3]

II. Recent Merger Enforcement Activity

In the past year, the Commission has challenged several mergers involving the pharmaceutical industry. Competition between producers of generic drugs often results in substantial savings for consumers who would otherwise have to purchase the brand-name equivalents. In 2006, the Commission investigated Watson Pharmaceuticals, Inc.'s acquisition of Andrx Corporation. Both companies were two of a small number of suppliers offering generic drugs used in the markets for oral contraceptives, treatment of acute pain, and Type 2 diabetes. Evidence indicated that unilateral and coordinated effects were likely to result from a reduction in the number of independent competitors, thereby increasing the likelihood that consumers would be forced to pay higher prices for generic drugs as result of the merger.[4]

The Commission challenged this transaction and required through a Commission order that, among other things, the parties divest rights and assets relating to the overlapping products to resolve the Commission's antitrust concerns. Interpharm and Actavis, the Commission-

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[2]FTC News Release, *FTC Chairman Announces Merger Review Process Reforms* (Feb. 16, 2006), *available at* http://www.ftc.gov/opa/2006/02/merger_process.htm.

[3]*U.S. Dep't of Justice & Fed. Trade Comm'n, Commentary on the 1992 Horizontal Merger Guidelines* (Mar. 2006), *available at* *http://www.ftc.gov/os/2006/03/CommentaryontheHorizontalMergerGuidelinesMarch2006.pdf*.

[4]*In the Matter of Watson Pharms., Inc., and Andrx Corp.*, FTC Docket No. C-4172 (complaint), *available at* http://www.ftc.gov/os/caselist/0610139/0610139complaint.pdf.

approved acquirers of the divested assets, have the experience, know-how, and infrastructure necessary to restore any competition lost from the proposed merger.[5] The acquirers also do not themselves present competitive problems related to the relevant product markets.

In September 2007, the Commission challenged an illegal agreement between two dialysis clinic operators. The asset purchase agreement between American Renal Associates, Inc. ("ARA"), and Fresenius Medical Care Holdings ("Fresenius") had two components. First, the parties agreed that Fresenius would close three of its own clinics located close to a competing ARA clinic; and second, Fresenius agreed to sell five of its Rhode Island clinics to ARA.[6]

The Commission charged first that the agreement between the parties – competitors in the provision of outpatient dialysis services – to close three Fresenius clinics was a horizontal agreement to eliminate competition and to reduce capacity in the affected areas. Agreements to pay a competitor to exit a market such as this are per se unlawful. Second, the Commission charged that ARA's proposed acquisition of two of Fresenius' clinics would eliminate direct competition in the market for outpatient dialysis services in the affected area. After FTC staff raised concerns about the agreement, the parties terminated the agreement. The Commission settled the antitrust charges through a consent order that prohibits the parties from agreeing with any person to close a dialysis clinic and compels the parties to notify the Commission of any

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[5]*In the Matter of Watson Pharms., Inc., and Andrx Corp.*, FTC Docket No. C-4172 (finalized Dec. 12, 2006) (decision and order), *available at* http://www.ftc.gov/os/caselist/0610139/061212do_public_ver0610139.pdf; *In the Matter of Watson Pharms., Inc., and Andrx Corp.*, FTC Docket No. C-4172 (analysis), *available at* http://www.ftc.gov/os/caselist/0610139/0610139analysis.pdf.

[6]*In the matter of American Renal Associates, Inc.*, FTC File No. 051-0234 (analysis), *available at* http://www.ftc.gov/os/caselist/0510234/070907analysis.pdf.

future plans to acquire dialysis clinics in the relevant area.[7]

In June 2007, acting to ensure that consumers continue to have a choice in where they shop for prescription drugs, the Commission challenged the proposed merger between Rite Aid Corporation and the Brooks and Eckerd pharmacy chains owned by Jean Coutu Group, Inc. The Commission alleged that the relevant product market – the retail sale of pharmacy services to cash customers – was highly concentrated. Customers viewed Rite Aid and Eckerd/Brooks as their first and second choices in 23 local markets. Furthermore, the Commission charged that entry was unlikely.[8] To restore pre-merger competition for pharmacy services to cash customers, the parties are obligated under the FTC consent order to sell one store in each overlap market to a Commission-approved acquirer.[9]

In the area of military defense, in 2006, the Commission challenged the proposed acquisition of SNC Technologies, Inc., and SNC Technologies, Corp., by General Dynamics. General Dynamics, through its interest in American Ordnance, and SNC were two of only three companies that contracted with the U.S. military for the provision of melt-pour load, assemble, and pack (LAP) services used for mortar rounds and artillery shells. The proposed combination raised the incentives for General Dynamics to unilaterally increase prices, and also raised the

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[7]*In the matter of American Renal Associates, Inc.*, FTC File No. 051-0234 (decision and order), *available at* http://www.ftc.gov/os/caselist/0510234/070907order.pdf.

[8]*In the matter of Rite Aid Corporation and The Jean Coutu Group (PJC), Inc.*, FTC File No. 061-0257 (analysis), *available at* *http://www.ftc.gov/os/caselist/0610257/070604analysis.pdf*.

[9]*In the matter of Rite Aid Corporation and The Jean Coutu Group (PJC), Inc.*, FTC File No. 061-0257 (finalized Sept. 21, 2007) (decision and order), *available at* http://www.ftc.gov/os/caselist/0610257/070921decision.pdf.

likelihood of coordination between the remaining competitors in the LAP services market.[10] To alleviate anticompetitive concerns, General Dynamics had to divest, under the FTC consent order, its interest in American Ordnance to an independent competitor.[11]

The petroleum industry represents an important part of the U.S. economy. Protecting consumers from the effects of anticompetitive mergers in the energy sector is a focus of much of the Commission's efforts. Thus far in 2007, the Commission has brought two preliminary injunctions actions to block two proposed mergers in the oil and gas industry.

In the spring of 2007, the FTC filed a complaint in the U.S. District Court in Western District of Pennsylvania against the proposed acquisition of the Peoples Natural Gas Company, a subsidiary of Dominion Resources, by Equitable Resources, Inc. In the complaint, the Commission alleged that Equitable and Dominion Peoples were each other's sole competitors in the distribution of natural gas to nonresidential customers in certain areas of Allegheny County, Pennsylvania, which includes Pittsburgh. Although the Pennsylvania Public Utilities Commission (PUC) sets the ceiling for rates companies can charge for natural gas, Equitable Dominion and Peoples competed by offering discounts below the maximum rates. Thus, the pending transaction is likely to result in a monopoly for nonresidential customers, who no longer would have a choice between the two companies for receiving their natural gas.[12]

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[10] *In the Matter of General Dynamics Corp.*, FTC Docket No. C-4181 (Feb. 7, 2007) (complaint), *available at* http://www.ftc.gov/os/caselist/0610150/0610150complaint.pdf.

[11] *In the Matter of General Dynamics Corp.*, FTC Docket No. C-4181 (Feb. 7, 2007) (decision and order), *available at* http://www.ftc.gov/os/caselist/0610150/0610150decisionorder.pdf.

[12] *FTC v. Equitable Resources, Inc., Dominion Resources, Inc., et al.*, No. 07-cv-490 (W.D. Pa. filed April 13, 2007) (complaint filed), *available at* http://www.ftc.gov/os/adjpro/d9322/070413cmpltforpi-tro.pdf.

After conducting its own review, the PUC approved the merger.[13] Denying the Commission's request for a preliminary injunction, the district court held that the state action doctrine bars the Commission from taking action regarding the merger because the PUC's approval of the merger qualified for state action immunity.[14] The Third Circuit has granted an injunction pending appeal.[15]

In its most recent challenge within the oil and gas industry, the Commission filed a complaint to enjoin Western Refining, Inc.'s proposed acquisition of Giant Industries, Inc. The FTC contended that both parties competed in the market for bulk supply of light petroleum products to northern New Mexico. The complaint further charged that, but for the proposed acquisition, Giant would increase the supply of gasoline to northern New Mexico, which would likely lead to a decrease in prices of bulk light petroleum.[16] The Commission's request for a preliminary injunction was denied by the U.S. District Court for the District of New Mexico.[17]

Also in 2007, the Commission challenged the merger between Whole Foods Markets, Inc., and Wild Oats Markets, Inc. In the complaint, the FTC alleged that in many local markets

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[13]*See*, http://www.puc.state.pa.us/general/press_releases/press_releases.aspx?ShowPR=1729.

[14]*F.T.C. v. Equitable Resources, Inc., Dominion Resources, Inc., et al.*, No. 07cv0490, 2007 WL1437447 (W.D.Pa. May 17, 2007).

[15] *FTC v. Equitable Resources, Inc., Dominion Resources, Inc., et al.,* No. 07-cv-490 (W.D. Pa. filed May 21, 2007) (order granting injunction pending appeal), *available at* http://www.ftc.gov/os/caselist/0610140/070601order.pdf.

[16]*FTC v. Paul L. Foster, Western Refining, Inc., and Giant Industries, Inc.*, No. 07-cv-00352 (D. N.M. filed April 12, 2007) (complaint filed), *available at* http://www.ftc.gov/os/caselist/0610259/070412western-giantcmplt.pdf.

[17]*F.T.C. v. Foster*, No. 07-352, 2007 WL 1793441 (D.N.M. May 29, 2007)

across the U.S., Whole Foods and Wild Oats were each other's closest competitors in the market for premium natural organic supermarkets.[18] The U.S. District Court for the District of Columbia denied the Commission's request for a preliminary injunction.[19]

II. Improvements to the Merger Review Process

The HSR merger review process is the primary method used by the Commission to investigate and analyze mergers. The Commission's goal is to utilize a process that is both rigorous and effective in protecting consumers from harmful mergers. Under the current trend, the enforcement agencies and the courts have moved away from structural presumptions such as market shares for determining whether a merger is likely to be anticompetitive and have moved towards a more integrated approach to analyzing competition in the markets at issue in the proposed merger. This approach has led to an ever-increasing demand by the Commission and the Department of Justice's Antitrust Division for more information from the parties and, in particular, an increase in the amount of data needed to perform sophisticated economic analyses.

The Commission recognizes, however, the burdens such demands impose on the parties involved. To examine ways in which these burdens could be reduced, Chairman Majoras initiated a thorough review of the process, incorporating expertise from all levels of the Commission.[20] The project resulted in reforms to the second request process, formally issued in

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[18] *FTC v. Whole Foods Markets and Wild Oats Markets*, No. 1:07-cv-01021 (D.D.C. filed June 5, 2007), (complaint filed), *available at* http://www.ftc.gov/os/caselist/0710114/070605complaint.pdf.

[19] *F.T.C. v. Whole Foods Market, Inc.*, 2007 WL 2377000 (D.D.C. August 16, 2007).

[20] *Interview with Deborah P. Majoras, Chairman, Federal Trade Commission*, The Antitrust Source, March 2005, at 2-3.

2006 ("2006 Reforms")[21], as well as the introduction of electronic filing procedures for the HSR premerger notification forms.[22] Collectively, the 2006 Reforms and electronic filing procedures serve to streamline the process and reduce the cost, in both time and money, associated with complying with HSR requirements.

One significant component of the 2006 Reforms is the custodian presumption.[23] FTC staff agree to limit the number of persons whose files need to be searched for responsive documents to 35 employees. The presumptive 35 employee limit does not apply to documents requested from "central" files or "corporate" files, regardless of whether the documents ultimately may come from the employees already in the search group. Also, if Commission staff determine that a larger group is warranted to investigate the transaction, staff may request authorization from the Bureau Director to exceed the 35 employee limitation.

To opt in to this presumption, the parties must provide organizational charts and, if requested, written job descriptions of employees. The parties must also continue to make available to Commission staff, company employees who can assist staff in designating the 35 custodian employees with the most relevant documents. Also, the parties must enter into a timing agreement with FTC staff regarding the document submission. Usually, this constitutes a rolling production agreement where the parties produce responsive materials over an agreed-

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[21]Federal Trade Commission, *Reforms to the Merger Review Process* (Feb. 16, 2006), *available at* http://www.ftc.gov/os/2006/02/mergerreviewprocess.pdf.

[22]FTC News Release, *Federal Trade Commission and Department of Justice Allow Electronic Submission of Premerger Notification Forms* (June 20, 2006), *available at* http://www.ftc.gov/opa/2006/06/premerger.shtm.

[23]Federal Trade Commission, *Reforms to the Merger Review Process* (Feb. 16, 2006), at 9-11, *available at* http://www.ftc.gov/os/2006/02/mergerreviewprocess.pdf.

upon timeframe. Furthermore, for parties electing to utilize the custodial presumption, if Commission decides to litigate a challenge to the merger, the parties agree to propose jointly with the FTC, a scheduling order with at least 60 days for discovery.

Another important change to the merger review process under the 2006 Reforms is the two-year relevant time period presumption.[24] Under this presumption, the relevant time period for an FTC second request (the time period from which parties will be required to submit documents) will be from two years prior to the date on which the FTC issues the second request until 45 days prior to certification of substantial compliance with the second request. The time limitation does not apply to data requests, since the Commission recognizes that economic analysis often requires years of historical data. Additionally, Commission staff may extend the relevant period if it believes that the analysis of a particular merger necessitates a review of documents from a longer period of time. This reform may generate significant reductions in cost of complying with second requests that previously usually required responsive material for a three-year relevant time period.

The 2006 Reforms also require FTC staff to inform the parties about the competitive effects theories under consideration by the agency and about the types of empirical analyses that may prove useful in the investigation.[25] The exchange of information contemplated under this reform facilitates open communication between Commission staff and the parties, as the parties are encouraged to share how their data is collected, used, and maintained, and to provide access to employees knowledgeable about the data. The parties are entitled to meet with the Director or

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[24] *Id*. at 19.

[25] *Id*. at 21-22.

Deputy Directors from the Bureau of Competition and the Bureau of Economics if they believe that the data demands under the second requests are too broad.

The 2006 Reforms also amend the requirements regarding privilege logs.[26] Previously, under the Model Second Request, parties were required to produce a complete log of all responsive documents withheld on the basis of privilege. Following the 2006 Reforms, Commission staff will allow the parties to elect to produce a partial privilege log for all of the custodians in the party's search group. If the party opts to submit a partial privilege log, FTC staff may require a complete privilege for a small subset of those employee custodians. Commission staff may also request a complete log for all custodians in certain circumstances, such as if the Commission decides to litigate a challenge to a proposed merger. This reform is designed to lower the costs associated with compiling a complete privilege log where the benefits of the log do not outweigh the burdens of production.

As part of the ongoing process of adapting to new technology, FTC second requests now enable parties to elect to provide electronic copies of original documents. Parties are required to discuss the form and method of their electronic document production with Commission staff. Included in the accepted forms of document production are CD-ROM, DVD-ROM, and USB hard drives.

In addition to procedural and technical adjustments to the second request process, the FTC and Antitrust Division have enhanced the transparency of the analytical process through which the agencies review mergers by issuing the Commentary on the Guidelines. The Commentary addresses almost all aspects of the Merger Guidelines - market definition and

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[26] *Id*. at 25.

concentration, coordinated interaction, unilateral effects, entry, and efficiencies. It provides specific examples of how the enforcement agencies employ the Merger Guidelines in actual investigations, and identifies areas where the agencies go beyond the text of the Guidelines to assess the legality of particular transactions. Combined with the 2006 Reforms, practitioners may find the Commentary useful in facilitating their communication with Commission staff regarding competitive effects theories and other arguments pertaining to the facts of their particular transaction.

IV. Conclusion

The FTC continues to be active in its mission to protect consumers from mergers that violate antitrust laws. At the same time, the Commission strives to improve the process through which mergers are reviewed so as to reduce the amount of resources necessary to complete the investigation of a proposed transaction. While navigating the merger waters at the FTC may continue to present substantive and procedural challenges, the 2006 Reforms and other improvements are likely to ensure the efficiency of the process.