COMMENTS OF THE AMERICAN BAR ASSOCIATION ANTITRUST LAW SECTION ON THE U.S. ANTITRUST AGENCIES' DRAFT VERTICAL MERGER GUIDELINES

February 22, 2020

The views stated in this submission are presented on behalf of the Antitrust Law Section. They have not been approved by the House of Delegates or the Board of Governors of the American Bar Association and therefore should not be construed as representing the policy of the American Bar Association.

The American Bar Association Antitrust Law Section ("the Section") commends the Department of Justice and the Federal Trade Commission ("the Agencies") for providing the opportunity to comment on their Draft Vertical Merger Guidelines ("VMGs"). This comment reflects the expertise and experience of the Section's members with antitrust law and economics.

EXECUTIVE SUMMARY

The Agencies have previously recognized that "vertical mergers merit a stronger presumption of being efficient than do horizontal mergers, and should be allowed to proceed except in those few cases where convincing, fact-based evidence relating to the specific circumstances of the vertical merger indicates likely competitive harm."[1] With this in mind, the Section offers the following recommendations to further improve and clarify certain principles in the VMGs, which would provide additional clarity and predictability for stakeholders:

§§ 2-3. Market Definition and Related Products; Market Participants, Market Shares, and Market Concentration

- Increase the 20 percent quasi-safe harbor to a number in the range of 30 to 40 percent and strengthen the language to provide greater certainty. Specifically, add the following sentence: "Vertical mergers with shares below these levels likely require no further analysis," and reduce the last paragraph of Section 3 to the sentence: "Vertical mergers above these levels might require further analysis but are not inherently suspect." These changes would provide increased predictability for stakeholders, minimize deterrence of procompetitive deals, and bring the VMGs more in line with international norms and Agency practice.

- Clarify the analysis for defining "related product" markets. For example, specify whether there are situations under which a full market definition is required; the required degree of direct or indirect "relatedness;" and when transactions that do not involve adjacent, linearly-related firms may fall within the provision.

[1] OECD, Competition Policy Roundtables, Vertical Mergers, 239 (2007), *available at* https://www.oecd.org/competition/mergers/39891031.pdf.

§ 5. Unilateral Effects

- Clarify that the relevant inquiry for raising rivals' costs ("RRC") is the effect on downstream competition.

§ 6. Elimination of Double Marginalization

- Explicitly recognize that (1) elimination of double marginalization ("EDM") is unique among merger benefits in its connection to vertical mergers and RRC and its likelihood of (at least in part) coinciding with RRC; (2) the difficulties of achieving EDM through contract; and (3) while evidence of EDM should involve documentation by the merging parties, analysis of its existence and extent should more closely follow that of RRC when the incentive and ability to achieve EDM is established (*e.g.*, the Agencies may require less extensive documentation compared with what is typically required for the types of efficiencies set forth in Section 8 of the VMGs).

- Explicitly state that a preexisting contract will not be treated as conclusive evidence that vertical integration is unnecessary, and may in fact be evidence to the contrary.

§ 8. Efficiencies

- Expand the efficiencies section to begin with a discussion of the coordination problems associated with vertical dealing and how vertical integration works to solve these problems.

SPECIFIC COMMENTS

While the Section applauds the Agencies' efforts to explain the theories of competitive harm that may result from vertical mergers, the VMGs, unlike the Horizontal Merger Guidelines ("HMGs"), provide little practical guidance to business on how the Agencies will distinguish between pro- and anticompetitive vertical deals, or how they will apply and test vertical theories. The HMGs and decades of court precedent provide practical guidance to business to predict (with the help of experienced antitrust practitioners) whether a horizontal transaction is likely to raise competition concerns. Doing the same for vertical mergers may not be possible given the lack of consensus (and the state of our economic toolkit) on the circumstances or evidence under which vertical mergers are likely to be anticompetitive. For example, leading economists have noted that vertical merger simulations are sensitive to assumptions, and economic models are easy to challenge.[2] Analysis of a specific vertical merger may turn largely on the unique facts concerning that transaction, complicating its utility as precedent.

[2] FTC, Hearing # 5 on Competition and Consumer Protection in the 21st Century, Presentation ("*Presentation*"), at 81 (Slade) (Nov. 1, 2018), *available at* https://www.ftc.gov/system/files/documents/public_events/1415284/ftc_hearings_5_georgetown_slides.pdf ("Vertical merger simulations will be even more sensitive to assumptions[;] I am skeptical about our ability to obtain precise numbers for merger costs and benefits."); *Presentation*, at 100 ("But given current state of theory and empirical evidence, guidelines are not what I would propose. Rather, look to academic community and perhaps some specific cases (e.g., AT&T/TW) to develop better understanding and clear tests and analyses to predict effects; not there yet in my view.").

Some context is important. Between 1994 and July 2018, the DOJ and FTC challenged at most 58 mergers (approximately 2.5 per year) that involved vertical concerns (many of these also involved horizontal concerns).[3] Over roughly the same period, the DOJ challenged a total of more than 550 mergers[4] and the FTC challenged a total of more than 560 mergers.[5] This means that between 1994 and 2018, mergers that involved vertical concerns comprised at most 5% of the DOJ's and FTC's merger cases that resulted in in-depth review. In our experience, since the DOJ's challenge to *AT&T/Time Warner*, few topics in antitrust have raised as much concern or as many questions from business as vertical merger policy.

In recent years, extensive thought, discussion, and review of vertical mergers has occurred among antitrust Agencies, and a number of vertical mergers have been closely scrutinized by various antitrust agencies. For example, the U.S. Agencies recently opened in-depth investigations of the AT&T/Time-Warner, Aetna/CVS, United Health Group/DaVita Medical Group, and Staples/Essendant transactions, to determine whether the vertical effects of those deals substantially lessened competition.[6] The economic theories of harm identified by the Agencies in these cases—input and customer foreclosure (either complete, partial, or in the form of "raising rivals' costs"[7])—are well understood in the academic literature.[8] So too are economic theories of vertical effects in direct price-setting environments and bargaining environments, among many others. The Section observes that the VMGs adhere to a generally accepted set of vertical merger economic concepts.

Vertical mergers can also engender many competitive and consumer benefits. There is a rich economic literature on the "theory of the firm" as it concerns the determinants of vertical firm structures, and vertically merged firms may benefit end consumers through reduced pricing (via EDM), streamlined operations, and enhanced scale and scope. Literature suggests these benefits from vertical mergers can potentially offer significant and direct increases to consumer welfare, which can potentially outweigh the harmful foreclosure effects of vertical mergers.[9]

[3] Steven C. Salop and Daniel P. Culley, *Vertical Merger Enforcement Actions: 1994-July 2018* (2018), Georgetown Law Faculty Publications and Other Works, *available at* https://scholarship.law.georgetown.edu/cgi/viewcontent.cgi?article=2541&context=facpub.

[4] DOJ Workload Statistics, *available at* https://www.justice.gov/atr/division-operations.

[5] FTC Annual Competition Reports, *available at* https://www.ftc.gov/policy/reports/policy-reports/annual-competition-reports.

[6] For a summary of the economic literature, see Statement of Commissioner Noah Joshua Phillips and Commissioner Christine S. Wilson, In the Matter of UnitedHealth Group and DaVita, FTC File No. 181-0057 (June 19, 2019), *available at* https://www.ftc.gov/system/files/documents/public_statements/1529366/181_0057_united_davita_statement_of_cmmrs_p_and_w.pdf.

[7] *Id*.

[8] *See, e.g., Presentation, supra* n. 2, at 5-57 (Salop).

[9] *Presentation*, *supra* n. 2, at 59-68 (O'Brien); *id*. at 69-81 (Slade); *id*., at 83-100 (LaFontaine). *See also* FTC Hearing #5: Vertical Merger Analysis and the Role of the Consumer Welfare Standard in U.S. Antitrust Law (Nov. 1, 2018), *available at* https://www.ftc.gov/news-events/events-calendar/ftc-hearing-5-competition-consumer-protection-21st-century.

The challenge for competition enforcers is to provide guidance that helps separate anticompetitive vertical transactions from procompetitive transactions. This task is made more difficult by the lack of consensus on the circumstances, evidence, or indicia of the circumstances under which vertical mergers are likely to be anticompetitive. While under-enforcement against vertical mergers may restrain competition, over-enforcement, and even perception of over-enforcement, against vertical mergers also may have unintended consequences. For example, absent further guidance, companies may expend significant resources investigating and responding to vertical merger theories in transactions for which there is no practical anticompetitive effect and/or an insignificant vertical connection exists between the merging firms. Over-enforcement risks chilling investment, deterring procompetitive transactions, and unnecessarily discouraging R&D, to the detriment of long-term consumer welfare.

The Section, therefore, respectfully suggests that the VMGs would be strengthened by acknowledging in the Overview what the guidelines do (identify vertical theories of competitive harm) and what they don't do (provide practical indicia about how to distinguish procompetitive and anticompetitive vertical mergers or how to operationalize the theories because consensus around economic and legal principles on these issues do not yet exist). To address the other specific concerns, the Section offers the recommendations set forth below.

§§ 2-3. Market Definition and Related Products; Market Participants, Market Shares, and Market Concentration

The Section applauds the Agencies' efforts to draft guidance in the form of a screen to assist companies in evaluating this risk: "The Agencies are unlikely to challenge a vertical merger when the parties to the merger have a share in the relevant market of less than 20 percent, and the related product is used in less than 20 percent of the relevant market."[10] Screens can be very valuable tools.[11] However, the Section is concerned about the last paragraph in Section 3, which appears to negate any value that the 20 percent screen provides: "The purpose of these thresholds is not to provide a rigid screen to separate competitively benign mergers from anticompetitive ones. Rather, they provide one way to identify some mergers unlikely to raise

[10] VMGs, § 3.

[11] *See, e.g.*, "In the experience of the Section's members, a safe harbor can reduce transaction costs by providing parties with certainty and predictability for certain conduct. Where a safe harbor is rebuttable and it is difficult for parties to predict its application, the benefits of a safe harbor may be decreased." Comments of the American Bar Association Section of Antitrust Law to the Fiscalia Nacional Economica (FNE) of Chile on the Draft Guidelines for Vertical Restraints, 2 (Jan. 30, 2014), *available at* https://www.americanbar.org/content/dam/aba/administrative/antitrust_law/at_comments_fiscalia_chile.pdf; "The Draft Guidelines state that a market share of 'less than 35 percent will typically not prompt further examination of whether the firm possesses market power,' but allow that a firm with a market share of 'less than 35 percent could have some degree of unilateral power in some instances, depending on the characteristics of the relevant market.' The Sections are concerned that the uncertainty introduced by this language negates the value of the 35% safe harbor, which may not be considered a safe harbor at all. In particular, further guidance on what sorts of 'characteristics of the relevant market' would indicate that a firm with limited market share could nevertheless amass market power would provide important assurance for firms and practitioners." Joint Comments of the American Bar Association Section of Antitrust Law and Section of International Law (The Sections) on the Canadian Competition Bureau's Draft Enforcement Guidelines for Price Maintenance (Section 76 of the Competition Act) (The Draft Guidelines) (June 2, 2014), *available at* https://www.americanbar.org/content/dam/aba/administrative/antitrust_law/at_comments_201406_rpm.pdf.

competitive concerns and some others for which it is particularly important to examine other competitive factors to arrive at a determination of likely competitive effects."[12]

Although the Section acknowledges that any particular numerical screen is subject to attack as arbitrary, and there may be extraordinary exceptions to any rule, the Section submits that the Agencies should adopt a higher relevant market share threshold and provide clearer guidance to business about the circumstances in which the Agencies will deviate from a screen. Such screens or thresholds are commonly adopted to create objective and easy to understand criteria that permit separating the transactions that may raise major competition concerns from those with a minor potential to harm competition. As Table 1 demonstrates, a common thread among existing Agency guidelines across merger and non-merger enforcement is clear guidance about the circumstances in which the Agencies are not likely to investigate or challenge a merger or conduct, and the rare instances in which they are likely to deviate from any screen. Consistent with the guidelines in Table 1, and to avoid chilling potentially benign or procompetitive vertical mergers, the Section recommends that the Agencies revise the Guidelines to (1) adopt a clearer screen, and (2) delineate the circumstances in which they are likely to deviate from the screen.

Table 1: DOJ and FTC Screens in Various Enforcement Guidelines

Guidance Document	Screen
HMGs	"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." "Mergers resulting in unconcentrated markets are unlikely to have adverse competitive effects and ordinarily require no further analysis." "The analysis in Section 7.2 applies to moderately and highly concentrated markets, as unconcentrated markets are unlikely to be vulnerable to coordinated conduct."

[12] *Id.*

DOJ and FTC Statements of Enforcement Policy in Health Care	"The Agencies will not challenge, absent extraordinary circumstances,[13] any joint purchasing arrangement among health care providers where two conditions are present: (1) the purchases account for less than 35 percent of the total sales of the purchased product or service in the relevant market; and (2) the cost of the products and services purchased jointly accounts for less than 20 percent of the total revenues from all products or services sold by each competing participant in the joint purchasing arrangement." "The Agencies will not challenge any merger between two general acute-care hospitals where one of the hospitals (1) has an average of fewer than 100 licensed beds over the three most recent years, and (2) has an average daily inpatient census of fewer than 40 patients over the three most recent years, absent extraordinary circumstances. This antitrust safety zone will not apply if that hospital is less than 5 years old."
DOJ and FTC Statements of Enforcement Policy in Health Care & DOJ and FTC Antitrust Guidance for Human Resource Professionals (incorporated by reference)	"The Agencies will not challenge, absent extraordinary circumstances, provider participation in written surveys of (a) prices for health care services, or (b) wages, salaries, or benefits of health care personnel, if the following conditions are satisfied: (1) the survey is managed by a third-party (e.g., a purchaser, government agency, health care consultant, academic institution, or trade association); (2) the information provided by survey participants is based on data more than 3 months old; and (3) there are at least five providers reporting data upon which each disseminated statistic is based, no individual provider's data represents more than 25 percent on a weighted basis of that statistic, and any information disseminated is sufficiently aggregated such that it would not allow recipients to identify the prices charged or compensation paid by any particular provider."

[13] "The Agencies are confident that conduct falling within the antitrust safety zones contained in these policy statements is very unlikely to raise competitive concerns. Accordingly, the Agencies anticipate that extraordinary circumstances warranting a challenge to such conduct will be rare." *Available at* https://www.justice.gov/atr/page/file/1197731/download.

FTC and DOJ Antitrust Guidelines for Collaborations Among Competitors	"Absent extraordinary circumstances, the Agencies do not challenge a competitor collaboration on the basis of effects on competition in an innovation market where three or more independently controlled research efforts in addition to those of the collaboration possess the required specialized assets or characteristics and the incentive to engage in R&D that is a close substitute for the R&D activity of the collaboration." "Absent extraordinary circumstances, the Agencies do not challenge a competitor collaboration when the market shares of the collaboration and its participants collectively account for no more than twenty percent of each relevant market in which competition may be affected."
Antitrust Guidelines for the Licensing of Intellectual Property	"Absent extraordinary circumstances, the Agencies will not challenge a restraint in an intellectual property licensing arrangement that may affect competition in a technology market if (1) the restraint is not facially anticompetitive and (2) there are four or more independently controlled technologies in addition to the technologies controlled by the parties to the licensing arrangement that may be substitutable for the licensed technology at a comparable cost to the user." "Regarding potential effects in a research and development market, the Agencies, absent extraordinary circumstances, will not challenge a restraint in an intellectual property licensing arrangement if (1) the restraint is not facially anticompetitive and (2) four or more independently controlled entities in addition to the parties to the licensing arrangement possess the required specialized assets or characteristics and the incentive to engage in research and development that is a close substitute of the research and development activities of the parties to the licensing agreement."
DOJ and FTC Statement of Antitrust Enforcement Policy Regarding Accountable Care Organizations Participating in the Medicare Shared Savings Program	"This Section sets forth an antitrust safety zone for ACOs that meet the CMS eligibility criteria for and intend, or have been approved, to participate in the Shared Savings Program and are highly unlikely to raise significant competitive concerns. The Agencies will not challenge ACOs that fall within the safety zone, absent extraordinary circumstances."[14]

[14] "Extraordinary circumstances could include, for example, ACO participants engaging in collusion or improper exchanges of price information or other competitively sensitive information with respect to their sale of competing services outside the ACO." *Available at* https://www.justice.gov/sites/default/files/atr/legacy/2011/10/20/276458.pdf.

Like the DOJ and FTC, competition authorities around the world have also adopted screens for merger or other antitrust analysis, be it at the case submission phase or for deepening the analysis of notified matters. Table 2 below reports major jurisdictions that have share screens for vertical mergers.[15] Although the implications of the vertical merger thresholds in Table 2 vary,[16] they all suggest that vertical mergers below the clearly enumerated screen are not likely to lead to anticompetitive effects and therefore merit swift antitrust clearance. The screen in the draft VMGs is low, with an exception so broad that it creates divergence with these major jurisdictions and creates more uncertainty for business. Given the importance of the United States to global markets, the low screen is likely to have an outsized effect on the review of global transactions, possibly creating a chilling effect. The Section therefore recommends that the Agencies not adopt a share threshold that is lower and less clear than the thresholds in Brazil, China, the European Union, France, and Japan.

Table 2: Major Jurisdictions With Vertical Merger Thresholds

Jurisdiction	Vertical Merger Threshold	Summary
Japan	35%	In light of past cases, if the HHI is not more than 2,500 and the market share of the company group after the business combination is not more than 35%, the possibility that a business combination may substantially restrain competition is usually thought to be small.
EU	30%	The Commission is unlikely to find concern in non-horizontal mergers, be it of a coordinated or of a non-coordinated nature, when the post-merger market share of the new entity in each of the markets concerned is below 30% and the post-merger HHI is below 2,000.
France	30%	The Authority considers that it is unlikely that a company with market share of less than 30% of a relevant market could lock a market downstream or upstream of this one.
Brazil	30%	None of the applicants or their respective economic groups control more than 30% in any of the vertically integrated relevant markets.
China	25%	Vertical transactions in which share is less than 25% qualify for China's simplified procedure.

The Section also submits that the 20% threshold is inconsistent with case law and the Agencies' own practices. For example, in *AT&T/Time Warner*, the DOJ alleged that AT&T/DirectTV was the "largest participant in [the MVPD] product market in the United

[15] Jurisdictions such as Australia do not have delineated thresholds for vertical mergers. Canada has a 35% market share safe harbor applicable to all mergers, including vertical mergers. *Available at* https://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/03420.html.

[16] According to the thresholds in these jurisdictions, antitrust enforcers are unlikely to challenge a merger, unlikely to find anticompetitive effects, or the transaction qualifies for a "simplified" procedure, typically leading to quick clearance.

States," and "has more than 40 percent of MVPD subscribers in at least 18 local Designated Market Areas,"[17] including at least one zone with shares more than 80%.[18] Despite these shares, neither the district court nor the court of appeals found that substantial anticompetitive effects were likely. Likewise, in the last litigated FTC vertical merger challenge, the U.S. Court of Appeals for the Second Circuit rejected the FTC's challenge to Fruehauf Corporation's consummated acquisition of Kelsey-Hayes Company in which Kelsey-Hayes had a 32.5% share of the antiskid brake device market and Fruehauf had a 25% share of the downstream trailer market.[19] Although shares were not the exclusive reason that courts rejected these challenges, it is instructive that in the last two litigated challenges to vertical mergers, shares in excess of the ' proposed threshold failed to persuade courts to block the transactions.

The Section understands that the Agencies intended the VMGs to be descriptive of their existing practices with respect to vertical mergers. To that end, a review of the Agencies' vertical merger settlements from 2000 to the present reveals that, while there are a number of matters in which the Agencies did not allege market shares,[20] there does not appear to be even a single instance in more than 20 years in which the DOJ or FTC challenged a vertical merger that featured relevant market shares below 40%.[21] In most cases in which the DOJ or FTC reported shares, those shares exceeded 70%, which is consistent with the experiences of Section members who represent clients in front of the Agencies in vertical mergers.

The Section also recommends that the VMGs more clearly indicate that mergers below the proposed 30-40 percent range are "are unlikely to have adverse competitive effects and ordinarily require no further analysis," consistent with the application of market concentration screens in § 5.3 of the HMGs. In addition, the Section suggests that the VMGs should identify

[17] Complaint at 14, *U.S. v. AT&T Inc.*, 310 F.Supp.3d 161 (D.D.C. 2018), (No. 1:17-cv-02511), ("*AT&T/Time Warner*"), *available at* https://www.justice.gov/atr/case-document/file/1012916/download.

[18] Expert Report of Carl Shapiro at 182, *AT&T/Time Warner*, *available at* https://www.justice.gov/atr/case-document/file/1081336/download.

[19] *Fruehauf Corp. v. F.T.C.*, 603 F.2d 345, 349 (2d Cir. 1979).

[20] Even in settlements in which the DOJ or FTC did not allege shares, the agency implied that shares were very high. *See, e.g.*, Complaint at ¶ 30, *U.S. v. Premdor Inc.*, 1:01-CV-01696 (D.D.C. Aug. 3, 2001), *available at* https://www.justice.gov/atr/case-document/complaint-184 ("Only three firms make significant sales of interior molded doorskins in the United States. Two of those firms dominate the market--Masonite and the non-party firm."); Complaint at ¶¶ 16, 18, *In the Matter of The Boeing Company*, No. C-4188 (May 1, 2007), *available at* https://www.ftc.gov/enforcement/cases-proceedings/0510165/lockheed-martin-corporation-boeing-company-united-launch ("The U.S. markets for MTH Launch Services and Space Vehicles are highly concentrated. In the MTH Launch Services market, Boeing and Lockheed are the only competitors, and their consolidation will result in a monopoly. In the U.S. market for Space Vehicles, three firms, Boeing, Lockheed, and Northrop Grumman, account for the large majority of sales.").

[21] The one possible exception was the settlement in U.S. v. Graftech Int'l Ltd., 1:10-cv-02039 (D.D.C. Nov. 29, 2010), https://www.justice.gov/atr/case-document/complaint-116. In that matter, DOJ alleged an upstream relevant market share of 19% for the merging parties. The DOJ did not allege a downstream market but noted that the defendant was the "largest manufacturer" of products sold in the United States. DOJ's theory of harm was that the downstream firm's supply agreement with a competitor of the upstream firm included an MFN with audit rights that would provide the upstream firm with access to competitively sensitive information, enhancing potential for coordination. The competing upstream supplier had a 55% share in the relevant market. In a settlement, DOJ and the parties agreed to strike the audit rights and MFN from the supply contract.

all circumstances known to the Agencies in which they have or will deviate from the screen, understanding that new factual circumstances may arise.

In sum, given the Agencies' prior enforcement history, foreign jurisdiction screens, and the Section's past comments,[22] the Section recommends that the DOJ and FTC adopt a market screen that is in the range of 30-40 percent, consistent with the variety of precedents that are outlined herein, [23] below which the Agencies are unlikely to challenge a transaction absent extraordinary enumerated circumstances.[24]

The Section recommends that the VMGs identify why mergers below the proposed 30-40 percent screen are not likely to lead to anticompetitive effects and proposes the following examples:

> *Example 3:*[25] *Company A is a wholesale supplier of orange juice. It seeks to acquire Company B, an owner of orange orchards. Company B's market share in the supply of oranges to wholesalers is 30%. Because of its low market share in the supply of oranges, it is unlikely that the combined entity could foreclose or otherwise disadvantage Company B's competition.*
>
> *Example 4: Company A is a wholesale supplier of orange juice. It seeks to acquire Company B, an owner of orange orchards. Company A's market share in the purchase of oranges from orchards is 30%. Because of its low market*

[22] Joint Comments of the American Bar Association Section of Antitrust Law and Section of International Law on the Proposal of the European Commission for a Revised Block Exemption Regulation and Guidelines on Supply and Distribution Agreements at 7 (Sept. 1, 2009), https://www.americanbar.org/content/dam/aba/administrative/antitrust_law/comments_proposal-ec.pdf (advocating for a 40% screen for vertical agreements).

[23] *See Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2, 46-47 (1984) ("[T]he arrangement forecloses only a small fraction [30%] of the markets in which anesthesiologists may sell their services, and a still smaller fraction of the market in which hospitals may secure anesthesiological services."); ABA SECTION OF ANTITRUST LAW, ANTITRUST LAW DEVELOPMENTS § 1.D.2.b, 213-14 (8th ed. 2017) ("Since the early 1970s, judicial decisions have established a virtual safe harbor for market foreclosure of 20 percent or less. Although foreclosure of 20 to 30 percent was a gray area before *Jefferson Parish*, the concurring opinion in *Jefferson Parish*, which found exclusive dealing lawful without detailed analysis when 30 percent of the market was foreclosed, has led many courts to hold that higher market share thresholds are a prerequisite to finding exclusive dealing unlawful--and even then, a finding that the arrangement is anticompetitive is not a foregone conclusion.").

[24] The Section previously submitted comments to the European Commission on its draft guidelines that established 30% and 2,000 HHI thresholds below which non-horizontal mergers were unlikely to be anticompetitive were "too conservative, both qualitatively and quantitatively." Joint Comments of the American Bar Association's Section of Antitrust Law and Section of International Law on the European Commission's Draft Guidelines on the Assessment of Non-Horizontal Mergers Under the Council Regulation on the Control of Concentrations Between Undertakings (May 1, 2007), *available at* http://www.americanbar.org/content/dam/aba/administrative/antitrust_law/comments_assess-mergers.authcheckdam.pdf. The Section encourages economists and the Agencies to study whether this threshold should be adjusted upward or downward over time.

[25] We would recommend inserting these additional examples at the end of § 3.

share in the purchase oranges, it is unlikely that the combined entity could foreclose or otherwise disadvantage Company B's competition.

Example 5: Company A is a wholesale supplier of orange juice. It seeks to acquire Company B, an owner of orange orchards. Company A has a 95% share of the supply of oranges to manufacturers of orange flavor essence. Company A has just a 20% share of the supply of oranges for all uses in which oranges are reasonable substitutes. Because of A's low share in the overall supply of oranges, it is unlikely that the combined entity could foreclose or otherwise disadvantage the competition. Orange flavor essence manufacturers are not likely to suffer harm because they have numerous alternatives from which to purchase oranges.

Example 6: Company A is a wholesale supplier of orange juice. It seeks to acquire Company B, an owner of orange orchards. Even if Company A has a 70% share of wholesale orange juice supply, its acquisition of a Company B, which has a 5% share in orange orchards, is unlikely to cause anticompetitive harm.

Furthermore, the Agencies can further clarify their approach and/or specify when additional relevant market definitions are needed in review of a vertical merger. The Section recommends that the "related product" concept be clarified and respectfully observes that there are potentially unintended tradeoffs with regard to the current draft's approach to relevant market definition and "related product[s]."

First, the draft specifies that the Agencies "will normally identify one or more relevant markets in which the merger may substantially lessen competition" and – in addition – "will also specify one or more related products."[26] This approach takes an informal view of the related product: that one need not define the relevant market for this product. While this approach may help alleviate some burden on the Agencies and merging parties, since defining one or more additional relevant markets can be costly, time consuming, and potentially contentious, it may also, as stated in the draft, be impractical and present additional uncertainty in any vertical merger review. It may be the case that it is difficult to review certain vertical mergers without more fully defining a relevant market for the related product, in addition to the relevant market for the product facing a "lessen[ing of] competition."

Consider the following example that illustrates the problems that may arise in focusing only on one relevant product market definition.

Example 7: Company 1, a large upstream manufacturer, sells its product to ten equal-sized downstream firms, Companies A-J. Company 1 and Company A propose a vertical merger. Theories of harm for this setting might posit that the integrated Company 1-A will engage in input foreclosure or RRC against Companies B-J. These theories suggest that the lessening of competition occurs in the downstream market, making the downstream market the relevant antitrust

[26] VMGs, § 2.

market and the upstream product the "related" product. Moreover, in light of this relevant market definition, the vertical merger would be evaluated as having a 10% market share in the relevant market and as being "used in" up to 100% of the relevant market.

Without defining and evaluating the upstream market, it may not be clear in some cases whether the upstream firm has sufficient market power to engage in foreclosure or RRC. Some questions that might arise, though certainly not an exhaustive list: What are Company 1's direct competitors? What other upstream products (i.e., substitute inputs in production downstream) might exist? Over what time horizon has Company 1 held its share of the inputs downstream? What if the 100% "used in" share is transitory in nature? Practically speaking, it may not be possible to evaluate many or most vertical mergers without evaluation of these sorts of questions. But doing so is likely to be tantamount to completing the relevant market definition for the related product. As such, the Section suggests clarifying (a) what level of detail is typically required in evaluating the related product and (b) if (or when) there are common settings in which full relevant market definition is needed for the related product.

Second, the notion of "related" is not well defined in the VMGs. The Section suggests clarifying the directness and degree of "related-ness" that is required to trigger a review of a merger under these guidelines. What distinguishes "conglomerate" and "vertical" mergers? For example, would a merger of two downstream products that are complements to one another be considered "related" sufficiently to pull them under the purview of the VMGs?[27] If so, should complementary goods mergers be presumed procompetitive and, thus, different from other vertical mergers?[28]

As another example, if there are multiple steps to the notion of "related" (e.g., a three-level supply chain), how strongly must the merging products be linked?

Example 8: Company A sells a raw input to Company B. In turn, Company B processes the raw input and sells an intermediate good to Company C.

In the above example, does "related" apply to a merger of Companies A and C? Does the determination depend on information concerning Company B? Without further clarification in cases like those in the above examples and others, it is unclear what mergers, if any, are caught by the VMGs when the merging firms are not strictly adjacent in a linear supply chain.

[27] *Presentation, supra* n. 2, at 12 (Salop).

[28] Vertical Mergers: Is it Time for New Vertical Merger Guidelines?, *as part of* FTC Hearing #5 Transcript on Competition and Consumer Protection in the 21st Century ("*Transcript*"), at 40 (O'Brien) (Nov. 1, 2018) ("But there is a very important point here that no one should miss, and that is that just as a merger between two substitutes in a concentrated market puts upward pressure on price, a merger between two complements in concentrated markets puts downward pressure on certain prices. The math is actually identical except for the sine [sic] of the diversion ratio, which is positive in the case of substitutes and negative in the case of complements. So the logic that leads to, for example, a rebuttable presumption of harm for horizontal mergers in concentrated markets seems to suggest a rebuttable presumption of benefit for complements mergers in concentrated markets."), *available at* https://www.ftc.gov/system/files/documents/public_events/1415284/ftc_hearings_session_5_transcript_11-1-18_0.pdf.

§ 5. Unilateral Effects

The Section offers the following seven recommendations with respect to Section 5 on unilateral effects:

First, we respectfully urge the Agencies to clarify that the relevant inquiry for RRC is the effect on downstream competition and that raising the cost of an upstream input with no downstream effects does not reflect a merger that "substantially lessens competition" or "create[s] a monopoly." Upstream prices may increase post-merger for a variety of reasons, some of which cannot be characterized as an attempt to RRC. A cogent RRC theory of harm in merger control requires a demonstration that the merged entity has both the incentive and ability to RRC in order to exclude rivals. It also requires a showing that such a strategy is likely to be successful given the relevant legal and economic context.

In our experience, an inquiry into RRC's effect on downstream competition would reflect the Agencies' practice, including, for example, the approach taken by the DOJ in *AT&T/Time Warner*. In that case, the DOJ recognized that what matters is the effect on competition in the market in which the downstream firm competes, stating that "a vertically integrated firm may force its rivals to 'pay[] more to procure necessary inputs' ***and thus*** cause those rivals to increase their prices downstream.'"[29] The DOJ alleged harm to competition only in video distribution markets (*i.e.,* downstream markets), not the upstream programming market.[30]

Second, in a number of places, the VMGs seem to require a showing of ***either*** the incentive ***or*** the ability of the merged firm to engage in anticompetitive conduct. For example, Section 5.a. of the VMGs states that "the merger may increase the incentive or ability." Other sections seem to focus on incentives alone (*e.g.*, Section 7). We respectfully recommend that the Agencies clarify that both incentives ***and*** ability are required. Incentives are certainly important, particularly when considering procompetitive justifications given that, absent the incentive to engage in anticompetitive conduct, there must be a business reason to engage in the particular conduct. That said, without the ability, the merged party cannot cause harm. Requiring both incentive and ability gets us closer to the right answer on whether the conduct is actually anticompetitive.

This change would also bring the VMGs into alignment with prior Agency guidance, including the FTC's "Guide to Antitrust Law," which states that the "problem" with a vertical merger "mak[ing] it difficult for competitors to gain access to an important component product or to an important channel of distribution . . . occurs when the merged firm gains the ability ***and*** incentive to limit its rivals' access to key inputs or outlets."[31] This change would also create

[29] Joint Statement on Burden of Proof at Trial, *AT&T/Time Warner* (quoting *Sprint Nextel Corp. v. AT&T, Inc.*, 821 F. Supp. 2d 308, 330 at 6 (D.D.C. 2011)) (emphasis added), *available at* https://www.justice.gov/atr/case-document/file/1043756/download.

[30] Complaint at 13, *AT&T/Time Warner* (emphasis added), *available at* https://www.justice.gov/atr/case-document/file/1012916/download.

[31] Federal Trade Commission Guide to Antitrust Laws, Mergers, Competitive Effects (emphasis added), *available at* https://www.ftc.gov/tips-advice/competition-guidance/guide-antitrust-laws/mergers/competitive-effects.

consistency with the Agencies' Horizontal Merger Guidelines, which also recognize that both the ability and incentive is what matters.[32]

Third, the draft VMGs discuss the types of evidence the Agencies will consider in Section 4, and this is to be commended. The draft VMGs also list several conditions that are necessary for anticompetitive unilateral effects, such as that "[t]he magnitude of likely foreclosure or raising rivals' costs is not *de minimis* such that it would substantially lessen competition." The draft VMGs also comment on the potential use of merger simulation to determine the unilateral effects from a merger.[33]

The Section agrees that the Agencies should "not treat merger simulation evidence as conclusive in itself," since the results can be very sensitive to the different parameters and assumptions that are built into all of these models. In determining the ability and incentive for firms to increase prices, the 2010 HMGs suggest a variety of tests in addition to computer simulation models for evaluating the competitive effects of differentiated products merger, including a detailed discussion of diversion ratios and upward pricing pressure (Section 6.1). Will the Agencies use similar, simpler analyses when determining which vertical mergers to investigate? For example, will the Agencies perform an analysis that takes into account upstream and downstream margins, and diversion ratios from the target of RRC to the merging firm, or some other forms of analysis?[34] If so, then the draft VMGs should be more explicit in stating that.

Fifth, like the HMGs, the VMGs should reflect that competition is dynamic. As the HMGs acknowledge, "in some cases, non-merging firms may be able to reposition their products to offer close substitutes for the products offered by the merging firms . . . The Agencies consider whether repositioning would be sufficient to deter or counteract what otherwise would be significant anticompetitive unilateral effects from a differentiated products merger."[35] Likewise, the HMGs consider how incumbent firms may respond to changing competitive conditions, for example, by redirecting sales to a geographic market in response to a price increase.[36] The Section recommends that the VMGs consider typical responses from marketplace participants that can overcome potential anticompetitive effects. For example, a competitor foreclosed from an input may be able to backward integrate and/or self-supply. Likewise, a foreclosed competitor may be able to find ready sources of supply that it had not considered prior to the merger or substitute reasonably comparable alternatives. The Section recommends that the Agencies include in the VMGs the following examples:

[32] U.S. Dept. of Justice and Federal Trade Commission, Horizontal Merger Guidelines, ¶¶ 2.1.5, 5.2, 6.2 (August 2010), *available at* https://www.justice.gov/sites/default/files/atr/legacy/2010/08/19/hmg-2010.pdf.

[33] VMGs, § 5(a) ("[T]he Agencies may construct economic models designed to quantify the likely unilateral price effects resulting from the merger. These models often include independent price responses by non-merging firms.").

[34] *See*, for example, analyses proposed by Joshua S. Gans, *Concentration-Based Merger Tests and Vertical Market Structure*, 50 J.L. & ECON. 661 (2007) or Serge Moresi and Steven Salop, *vGUPPI: Scoring Unilateral Pricing Incentives in Vertical Mergers*, 79 ANTITRUST L.J. No. 1, at 185 (2013).

[35] HMGs, § 6.1.

[36] HMGs, § 5.2.

Example 11:[37] *Building off of Example 3, after the merged firm foreclosed its rivals, the rivals seek to import oranges from Mexico at a reasonably comparable cost (and/or suppliers in Mexico are attracted to a profit opportunity that previously did not exist in the U.S.). Prior to the merger, orange juice suppliers had not tried to import oranges from Mexico, but during its investigation, the Agency learns that orange juice suppliers can do so. With a new source of supply, rivals recapture lost sales from the merged firm, and prices in the orange juice market would likely return to premerger levels.*

Example 12: Building off of Example 3, if the merged firm were to foreclose its rivals (Companies C, D, & E), Company C is likely to purchase its own orange grove, Company D is likely to purchase a defunct orange grove, and Company E is likely to establish its own orange grove, which helps the rivals recapture lost sales from the merged firm. Within a brief period following the merger, prices in the orange juice would likely market return to premerger levels.

Example 13: Building off of Example 3, foreclosed rivals are unable to adequately source a sufficient supply of oranges to return prices to premerger levels in the orange juice market. However, during its investigation the Agency learns that rivals are capable of substituting a special mix of grapefruit and pineapple to replace the lost volume of oranges, resulting in a product of like grade and quality, that would likely help the rivals recapture lost sales from the merged firm, and return prices in the orange juice market to premerger levels.

§ 6. Elimination of Double Marginalization

The Section commends the Agencies on the VMGs' discussion of EDM separate and apart from other merger efficiencies. While EDM and other efficiencies both result in consumer benefits, EDM is unique in its close connection to theories of anticompetitive effects, in particular RRC. As such, the Section makes the following recommendations:

First, the Section suggests that the Agencies more explicitly acknowledge the close relationship between EDM and RRC. Among the reasons EDM is unique relative to other efficiencies: (a) EDM and RRC arise from fundamentally the same economic change and the two effects can, but not always, move together in a way that does not exist with other efficiencies; and (b) measurement of the two effects depends largely upon the same inputs for quantification. The Section recommends the Agencies more explicitly acknowledge these reasons in explaining why EDM is unique.[38]

[37] We would recommend inserting these examples after Examples 3-6 in the draft VMGs. Our example numbering assumes that you would add our other proposed examples.

[38] *Transcript*, *supra* n. 28, at 60 (Shapiro) ("So call that raising rivals' costs. That is inherent. And then also, there are some inherent efficiencies -- at least possible efficiencies including elimination of double marginalization. … So I think what is fundamentally different is that how do we handle the efficiencies in the vertical deals than horizontal, and we are hearing from panels about these inherent efficiencies, which economists would agree with, including me.").

The key structural change that can occur with a vertical merger is a combination of up- and downstream profit margins, *i.e.*, the merged firm is maximizing a single "pie" post-transaction. Joint profit maximization can induce the merged firm to lower its downstream prices through EDM, shifting consumer demand from rivals to the merged firm due to newly reduced prices. But the shift in rivals' consumer demand caused by EDM potentially affects the merged firm's incentive over whether to engage in RRC or not. For many vertical mergers, there can be both downward pricing pressure from EDM and upward pricing pressure from RRC.[39]

Moreover, beyond merely the fact that EDM and RRC are linked, present economic models show that EDM and RRC incentives can move together.[40] The ability to move together helps to increase the likelihood that, "where merger-specific EDM does occur, it can offset the incentives to raise the prices of the upstream and downstream merging firms."[41] To be clear, this

[39] To be clear, this is not a comment on the overall frequency of RRC or EDM effects across all vertical mergers generally. Rather, this discussion merely highlights the connection—at least in part—between the two effects, should they occur at all in a given case. It is also possible that vertical mergers may occur in competitive settings in which both RRC and EDM are not significant issues.

[40] *Presentation*, *supra* n. 2, at 62, 66-67 (O'Brien) ("Principle 1?–Harm from input foreclosure is more likely the greater is the market power of the upstream firm. But in canonical models, the benefits of vertical mergers tend to increase with upstream market power, too. … Principle 5?–Under bargaining, harm from input foreclosure is more likely the greater the value of diverted sales relative to the upstream margin. But in some canonical bargaining models with small upstream margins and high downstream margins, vertical mergers reduce prices. … And so on."); *Id.* at 92 (LaFontaine) ("Not clear more market power and high diversion ratios should make us worry more: in fact, with more market power, there is more scope for efficiencies."). *See also*, as examples of EDM and RRC moving together:

- The profits to the merging firm from RRC are usually increasing in the rate of diversion of sales from rival firms (e.g., high downstream diversion ratios toward the merged firm can raise incentives for RRC upstream). Moresi & Salop, *supra* n. 34, at 193 (Equation 1). But the benefits from EDM are also increasing in the rate of diversion of sales from rival firms. *Id.* at 204 (Equation 8).
- The profits to the merging firm from RRC are usually increasing in the downstream margin (e.g., each diverted downstream sale from rivals is relatively profitable to the merged firm). *Id.* at 193-194. But when high downstream margins exist, there are more likely to be large "double margins," presenting greater opportunity for benefits for EDM. *Id*. at n. 4 (discussing this concept and citing to Tirole (1988)).

[41] Moresi & Salop, *supra* n. 34, at 186. *See also*, Gloria Sheu & Charles Taragin, *Simulating Mergers in a Vertical Supply Chain with Bargaining*, 24-25 (U.S. Department of Justice, Economic Analysis Group Discussion Paper 17-3, Oct. 2017), *available at* https://www.justice.gov/atr/page/file/1011676/download ("Vertical mergers balance both benefits and costs, in the form of the elimination of double marginalization on the one hand, and raising rivals' cost on the other. … while vertical mergers can substantially harm consumers by raising rivals' cost, **[numerical simulation] indicates that on net the average vertical merger often yields relatively little consumer harm or even modest consumer benefit.** There exists substantial variation around the mean, however.") (emphasis added); Gregory S. Crawford et al., *The Welfare Effects of Vertical Integration in Multichannel Television Markets*, 86 ECONOMETRICA 891 (2018) (citing to pre-publication manuscript, *available at* https://www.nber.org/papers/w21832.pdf), 45 ("On average across all RSNs, the efficiency effects dominate the foreclosure effects when examining consumer and total welfare—both increase by approximately 1.3% and 0.6%, representing 15-16% of the total WTP generated by an RSN."); *Presentation, supra* n. 2, at 94-101 (LaFontaine) (citing other studies); Francine LaFontaine & Margaret Slade, *Vertical Integration and Firm Boundaries: The Evidence*, 45 J. OF ECON. LIT. 629 (2007) (citing to pre-publication manuscript, *available at* https://ageconsearchumn.edu/record/269756/files/twerp_799.pdf), 55 ("It is clear from the table that some authors have uncovered evidence of foreclosure. However, the existence of foreclosure is, by itself, insufficient to conclude that vertical integration is pernicious. Indeed, recall that Salinger's (1988) model shows that there are two countervailing factors associated with vertical mergers: an increase in foreclosure or other practices that disadvantage rivals and a lessening of double

is not to guarantee that EDM and RRC exactly cancel one another—the two incentives will often tend to move together, but which of the two is larger will be case-specific.

And as a more practical matter, the Agencies will tend to collect information that is probative of both EDM and RRC (and complete foreclosure) in the process of a typical investigation of a vertical merger. This reality is a close corollary of the relationship described above. Identifying and quantifying RRC depends on many of the same inputs that are used to identify and quantify EDM.[42] Thus, there is a practical consideration to quantifying EDM that is not necessarily present for other merger-related efficiencies.

Second, the Section observes that current economic literature explains that firms may generally find it difficult to achieve EDM (or other efficiencies for that matter) with contracts absent full vertical integration by merger.[43] Simple facts, such as the existence of contracts, are not in themselves sufficient evidence that firms have realized EDM under the pre-transaction status quo. Even with contracts in place pre-merger, various frictions may limit full realization of EDM, and vertical mergers may facilitate significantly greater efficiency.[44]

Given the apparent difficulty firms face in realizing EDM by contract and EDM's uniqueness relative to other efficiencies, the Section urges the Agencies to acknowledge that the ultimate proof of EDM may be somewhat different from other efficiencies. This is not to say that the merging firms have zero role in proving EDM. To the contrary, the merging firms are the best equipped to provide the inputs for quantifying EDM and are the best equipped in identifying conditions in which EDM is more likely (*e.g*., simple pricing pre-merger).

But unlike other efficiencies, the Agencies should give some leeway to instances in which the incentive and the ability to achieve EDM can reasonably be proven. The Section

marginalization or other practices that are inefficient. One must therefore balance the two. Two of the papers in the table attempt to assess that tradeoff (i.e., Mullin and Mullin (1997) and Chipty (2001)), and both conclude that efficiency gains outweigh foreclosure costs. The evidence in favor of anticompetitive foreclosure is therefore, at best weak, particularly when one considers that the industries studied were chosen because their vertical practices have been the subject of antitrust investigations.").

[42] *Presentation*, *supra* n. 2, at 79 (Slade); Moresi & Salop, *supra* n. 34, generally.

[43] *Presentation, supra* n. 2, at 88 (LaFontaine); *Transcript, supra* n. 28, at 73 (LaFontane) ("So let me summarize what I am trying to say about this. So for example, quantity forcing and two-part tariffs do not easily generate the same outcome as what a vertical merger could do because of demand uncertainty, risk aversion, information asymmetries, all sort of incentive problems."). *See also*, Francine LaFontaine & Margaret Slade, Inter-Firm Contracts, in 1 HANDBOOK OF ORGANIZATIONAL ECONOMICS 958 (Robert Gibbons & John Roberts eds., 2013), 976 ("Several studies of consequences consider how retail prices vary with contract choice (e.g., company ownership versus franchising with linear or affine prices versus spot market transactions). For example, Sheppard (1993) compares consumer prices for gasoline in leasee-dealer (contract) and company unites and finds evidence that, for some products, prices charged at leasee dealerships are higher. In contrast, Hastings (2004) makes a similar comparison and finds no difference in price levels.").

[44] *Presentation, supra* n. 2, at 88 (LaFontaine) (citing, e.g., the well-known example of GM/Fisher Body as an example where vertical restraints via contract failed to fully realize efficiencies, causing the firms to eventually merge); Jean Tirole, THE THEORY OF INDUSTRIAL ORGANIZATION 187-8 (1988) (explaining that it is difficult to design the optimal/efficient contract); Patrick Rey & Jean Tirole, *A Primer on Foreclosure*, HANDBOOK OF INDUSTRIAL ORGANIZATION 2154, 2160 (Richard Schmalensee & Robert Willig eds., 2014) (explaining that confidentiality and uncertainty may make it difficult to design an efficient contract).

urges the Agencies to acknowledge that the process by which EDM is proven should more closely follow that of RRC than that of other efficiencies. That is, where the incentive and ability to realize EDM *can* be demonstrated, it should be assumed that EDM *will* be realized at least to some degree, just as it is generally assumed RRC *will* be realized where the incentive and ability to do so can be demonstrated. This treatment is different from other efficiencies, where the Agencies generally require detailed plans of post-merger implementation to demonstrate the efficiencies *will* be achieved.[45]

Thus, the Section suggests the Agencies more explicitly acknowledge (1) EDM is unique among merger benefits in its connection to vertical mergers and RRC, and its likelihood of, at least in part, coinciding with RRC, (2) firms may struggle to achieve EDM through contract absent a merger and the mere presence of a contract may not prove EDM has already been achieved, and (3) the means by which EDM is proven should more closely follow that of RRC as compared to other efficiencies. The Section recommends that more concrete discussion of these observations be incorporated into the VMGs to provide clearer guidance as to how and why EDM is considered separate and apart from other merger-related efficiencies.

§ 8. Efficiencies

In addition to EDM, vertical mergers can achieve efficiencies such as quality improvements and faster and/or better innovation from coordination in product, design, and innovation efforts; and elimination of free-riding from harmonization of incentives. The Section recommends that the efficiencies section be expanded to include a robust discussion of these potential efficiencies. We also urge the Agencies to begin the efficiencies section with a more detailed discussion of the coordination problems raised by vertical dealing, and how they may be solved through vertical integration. In doing so, the Agencies could draw from their 2007 OECD paper on vertical mergers.[46]

As Ronald Coase explained in his classic 1937 study of the nature of the firm, there are transaction costs to market transactions; organizing economic activity within a firm can lower these costs and increase joint profits as compared to market transactions. Oliver Williamson emphasized the costs of "haggling" over "appropriable quasi-rents."[47] In addition to negotiation

[45] To this end, former Deputy Assistant Attorney General for Economics, Professor Carl Shapiro, explained that the manner by which EDM is proven ought to be more similar to RRC. *Transcript, supra* n. 28, at 61-63 (Shapiro) ("[W]e have to assume that the merged entity operates as a single entity to maximize overall profits and that means elimination of double marginalization. I do not think we have any alternative, as antitrust economists, to continue to assume that in all merger analysis that the merged entity operates as a unified entity that maximizes overall profits. . . . So that gives this elimination and that does create this efficiency. So, the key question then is, is it merger-specific? It is not about verifiability.").

[46] OECD, Competition Policy Roundtables, Vertical Mergers, (February 15, 2007), *available at* https://www.ftc.gov/sites/default/files/attachments/us-submissions-oecd-and-other-international-competition-fora/07RoundtableonVerticalMergers.pdf.

[47] Oliver E. Williamson, *The Vertical Integration of Production: Market Failure Considerations*, 61(2) AM. ECON. R. 112-23 (1971), *available at* https://www.researchgate.net/publication/4733004_The_Vertical_Integration_of_Production_Market_Failure_Considerations; Williamson, *Transaction-Cost Economics: The Governance of Contractual Relations*, 22(2) J.L. & ECON. 233-261 (1979), *available at* https://pdfs.semanticscholar.org/c982/727420ca620043ce8aa1b8865d00755a984d.pdf.

and "ink" costs, as Benjamin Klein[48] and Kevin Murphy[49] explain, with specific investments and insufficient reputational capital, vertical contractual relationships also present "rigidity costs," including potential holdup problems associated with rigid and imperfect long-term contracts. Vertical integration facilitates coordination by reducing contractual specification, thereby reducing reliance on court enforcement to enforce incomplete, imperfect, and rigid long-term contracts.

Adding an explicit discussion of these principles would help to address the Section's concerns that the Guidelines are unclear on how the Agencies will implement the principles and distinguish between pro- and anticompetitive deals.

Miscellaneous

Given the Agencies' longstanding practice, the Section recommends that the VMGs be revised to explicitly state that the Agencies do not recognize "conglomerate effects" as a theory of merger harm. For example, the DOJ's 2001 note for the OECD's Roundtable on Portfolio Effects in Conglomerate Mergers explains that "there is no empirical support for the notion that size alone conveys any significant competitive advantage that is not efficiency-related."[50] The DOJ went on to say that one of the "problem[s]" with the theory that a merger may harm competition by facilitating the bundling of complementary products "is that it has been used in some cases to block mergers . . . on the basis of a theory of competitive harm that depends on a highly attenuated chain of causation that invites competition authorities to speculate about what the future is likely to bring."[51] The DOJ concluded by saying: "Such hypothetical possibilities would not support a challenge under Clayton Section 7, which requires a showing of a substantial probability that the merger will lessen competition. This requirement is a sound one—an effort to assess and weigh anticipated near term efficiency benefits against more speculative longerterm market power possibilities would carry a high risk of enforcement errors and of deterring economically desirable transactions."[52]

[48] Klein, *Fisher-General Motors and the Nature of the Firm,* 43(1) J.L. & ECON. (2000), *available at* https://poseidon01.ssrn.com/delivery.php?ID=316105111106004108005119104098028094097057069013079039085087069107105013122070093075054034098101102014042111116090078104105100037027053089084031114078082067119098037033035091070083016027013075023077018020110020119076070020023117002008090070123082007&EXT=pdf; Klein, *The Economic Lessons of Fisher Body-General Motors, International Journal of the Economics of Business,* 14(1) INT'L J. ECON. BUS.105-41 (2007), *available at* https://www.tandfonline.com/doi/abs/10.1080/13571510601141112.

[49] Kevin Murphy and Benjamin Klein, *Vertical Integration as a Self-Enforcing Contractual Arrangement*, 63 AM. ECON. REV. 112-23 (1971), *available at* https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1664138.

[50] OECD, *supra n.* 1, at 214; *see also* William J. Kolasky, Conglomerate Mergers And Range Effects: It's A Long Way From Chicago To Brussels (Nov. 9, 2001) *available at* https://www.justice.gov/atr/speech/conglomerate-mergers-and-range-effects-its-long-way-chicago-brussels ("To the extent the EU's conglomerate merger decisions rests on vague fears that the merged firm might engage in predatory pricing or unlawful tying, such conduct is best addressed when and if it occurs, rather than ex ante at the time of a merger when we have none of the facts we would need to determine whether the conduct, if it occurs, would, in fact, [be] anticompetitive.").

[51] OECD, *Supra* n. 1, at 214.

[52] *Id.* at 219.

CONCLUSION

The Section appreciates the opportunity to comment and welcomes the opportunity to discuss with the Agencies any comments or questions they may have. The Section would also appreciate the opportunity for Renata B. Hesse to speak on its behalf at the March 11, 2020 Workshop.