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

Writer's Direct Access
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**Re: Horizontal Merger Guidelines
HMG Revision Project – Comment, Project No. P092900**

Dear FTC/DOJ Merger Guidelines Working Group Members:

We appreciate the opportunity to respond to the request for views on the public comment version of the Horizontal Merger Guidelines (HMGs) issued on April 20, 2010. We support the approach taken in the draft HMGs embodying a more comprehensive approach to market definition, that is, consideration of, among other things, both upstream and downstream competitive effects while recognizing that market definition is only one component in evaluating potential competitive effects.

Our limited additional suggestion is that a statement be incorporated in the guidelines directly addressing the application of these principles to mergers involving vertically integrated entities. The addition of commentary on this point will enhance the clarity of the guidelines, provide guidance to parties considering a merger of vertically integrated entities and enable those parties, and others that rely on the guidelines, to anticipate how those mergers, as opposed to the manufacturer/supplier mergers that are the focus of the guidelines, will be evaluated.

We recognize that, for purposes of the narrative exposition, the analytical framework in the HMGs is presented from the perspective of a merger involving suppliers that sell their products and the potential impact of their planned merger on their direct customers. We also recognize that there is reference in the guidelines to buyer mergers and the explanatory language reflecting that the same analytical tools can be applied to potential competitive effects upstream or downstream to the merging parties. This language provides important guidance; however, the language does not address the approach that will be utilized when a merger involves both upstream and downstream competitive effects.

The only reference noted to vertically integrated firms appears in section 5.1 (Market Participants), and notes that “Vertically integrated firms are also included [as market participants] to the extent that their inclusion accurately reflects their competitive significance.” (p. 15). Mergers involving one or more vertically integrated firm are not unusual. Greater

discussion of the approach to such mergers is, accordingly, warranted. Transactions involving vertically integrated entities warrant careful consideration of multi-tiered markets or markets in which the merging parties may have both upstream and downstream market power or the facility to, as a combined firm, yield upstream and downstream competitive effects.

For example, assume that a merger involves competing retail outlets. The HMGs clearly call for an analysis of the impact of such a merger on the retail customers, who are the direct customers of the retailer. It is common, however, for large national retailers to have national distribution systems as well as manufacturing operations. For example, many supermarkets have their own dairy product, baked goods or other private label product production and/or supply facilities. Those operations compete, obviously, with products of other dairy and baked goods manufacturers, who, from this perspective, are both suppliers to the supermarkets as well as direct competitors. The notion that multiple markets may be at issue in a particular merger is not novel. It has been recognized in the merger situations discussed in our initial comments. As the public comments version of the HMGs states (p. 7):

Where analysis suggests alternative and reasonably plausible candidate markets, and where the resulting market shares lead to very different inferences regarding competitive effects, it is particularly valuable to examine more direct forms of evidence concerning those effects.

Based on these considerations, we recommend that the draft HMGs be revised to directly address the agencies' broad and flexible approach when vertical integration issues may be raised. Although there are a number of sections where such language might be added, a minor addition to section 4.0 (p. 8), may be sufficient (underlining indicates addition):

The Agencies implement these principles of market definition flexibly when evaluating different possible candidate markets. Transactions involving one or more vertically integrated entities are but one example of situations warranting an open and flexible analytical approach. In evaluating this category of mergers, the Agencies will adopt, as the circumstances warrant, a flexible approach that evaluates both upstream and downstream competitive effects. Relevant antitrust markets defined according to the hypothetical monopolist test are not always intuitive and may not align with how industry members use the term "market."

At a minimum, the Guidelines should include an explicit statement that alerts readers that the agencies will evaluate competitive effects in all potentially relevant markets, including upstream and downstream competitive 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.

In addition, while perhaps implicit in the proposed Guidelines and prior actions of the Agencies, it would be constructive to provide guidance with respect to the manner in which the Agencies will regard market shares where a merger may have upstream and downstream competitive effects. For example, in the FTC's Toys "R" Us investigation, the FTC found that despite (or more properly as a result of) Toys "R" Us' 20% market share in the downstream retail market it was able to exercise market power in the upstream supply market sufficient to alter the conduct of its suppliers and yield significant anti-competitive effects in both the upstream supply and downstream retail markets.¹ To the extent that the Agencies may identify the potential for the same types of competitive effects in mergers between parties with such "two-sided" market positions but without high market shares in both markets, it would be instructive to clarify that point in the Guidelines. To that end, it would be prudent to add a footnote to the passage cited above that reads as follows: "To the extent that a merger has the potential to have upstream and downstream competitive effects, the Agencies will not be limited to a rigid market share analysis but will analyze the circumstances to determine whether the potential to cause anti-competitive effects can be caused at lower market share thresholds." I appreciate the agencies' consideration of these comments. 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,

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¹ *In the Matter of Toys "R" Us, Inc.*, Docket No. 9278, 126 F.T.C. 415 (F.T.C.) (September 25, 1997), 126 F.T.C. 415 (1998), *aff'd*, *Toys "R" Us, Inc. v. FTC*, 221 F.3d 928 (7th Cir. 2000).