Public Comments of

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On

The U.S. Department of Justice and The Federal Trade Commission
Draft Vertical Merger Guidelines
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INTRODUCTION

We commend the DOJ and FTC for their work in composing these Draft Vertical Merger Guidelines (Draft VMGs). In replacing the now quite dated non-horizontal material in the 1984 Merger Guidelines,[1] the Agencies have taken a big step to refresh and clarify this important component of federal antitrust practice. With the aim of further enhancing the utility of the Draft VMGs, our comments identify a few areas in which we believe they could be improved. These include the following:

- Further Discuss the Relationship between Vertical and Horizontal Merger Analysis
- Clarify the Definition of the "Related Product" Concept
- Consider Whether the "Related Product" Must Be Defined
- Consider Questions Not Addressed by the "Related Product" Concept
- Preserve Flexibility in the Application of Quasi-Safe Harbors or Safety Zones
- Relocate Discussion of Evidence of Adverse Competitive Effects
- Eliminate Discussion of *De Minimis* Effects
- Resolve Inconsistent Assertions of Enforcement Likelihood
- Reconsider Weak Assertions of Enforcement Likelihood
- Relocate Discussion of EDM
- Clarify Distinctions between Vertical and Horizontal Coordinated Effects Analysis

[*] We submit these comments in our personal capacities. The views expressed in these comments do not purport to represent those of our employers, any institutions with which we are affiliated, or any of our clients.

[1] U.S. DEP'T OF JUSTICE, NON-HORIZONTAL MERGER GUIDELINES (1984) [hereinafter "1984 VMGs"] (originally issued as part of U.S. DEP'T OF JUSTICE, MERGER GUIDELINES § 4 (1984)), https://perma.cc/QHS8-6HDY.

SECTION 1. OVERVIEW

Further Discuss the Relationship between Vertical and Horizontal Merger Analysis

Readers of the VMGs would benefit from a more explicit identification and explanation of the close relationship between vertical and horizontal merger analysis.

As written, the Draft VMGs and the Horizontal Merger Guidelines (HMGs) could be read to present conflicting messages about the interplay between vertical and horizontal merger review. On the one hand, the Draft VMGs expressly state that they should be read in conjunction with the HMGs,[2] and incorporate several aspects of the HMGs by reference.[3] On the other hand, both the HMGs and Draft VMGs disclaim overlapping coverage in their first footnotes.[4] While these are not inconsistent propositions, we worry that non-expert readers might misinterpret these guidelines as suggesting a more siloed analytical approach than we expect the Agencies to take. Proposed mergers may present both horizontal and vertical elements,[5] and the Draft VMGs and HMGs should provide a clear, consistent message about how the Agencies will apply these frameworks in addressing the different elements of such mergers.

We suggest that the VMGs note, in Section 1, the similarity between, and overlapping concerns of, vertical and horizontal merger analysis. All vertical-merger concerns are ultimately horizontal in nature.[6] We believe that incorporating some version of the following clarifying observations would benefit non-expert readers of this section.

- *Some acquisitions present both horizontal and vertical elements. When the Agencies review an acquisition for competitive concerns, they may analyze its horizontal elements, vertical elements, or both.* For example, an acquisition might raise coordination concerns on both horizontal and vertical grounds. When this is the case, the Agencies may analyze the acquisition under the framework of both the HMGs and the VMGs.

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[2] U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, DRAFT VERTICAL MERGER GUIDELINES § 1 ¶ 2 (Jan. 10, 2020) [hereinafter "DRAFT VMGS"], https://perma.cc/9Y99-WBQ9 ("These Guidelines should be read in conjunction with the Horizontal Merger Guidelines.").

[3] *E.g.*, *id.* at § 1 ¶ 2; *id.* at § 2 ¶ 1; *id.* at § 3 ¶ 2; *id.* at § 4 ¶ 1; *id.* at § 7 ¶ 1.

[4] *See* U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, HORIZONTAL MERGER GUIDELINES § 1 n.1 (2010) [hereinafter "HMGs"], https://perma.cc/6S9W-T3JA ("These Guidelines do not cover vertical or other types of non-horizontal acquisitions."); Draft VMGs, *supra* note 2, at § 1 n.1 ("These Guidelines do not cover horizontal or other types of non-vertical acquisitions.").

[5] *See, e.g.*, Steven C. Salop, *Invigorating Vertical Merger Enforcement*, 127 YALE L.J. 1962, 1964 (2018) (discussing the presence of horizontal overlaps in some challenged mergers involving vertical integration). While intuitive examples today include mergers of technology and healthcare companies, transactions involving both vertical and horizontal elements are hardly a recent phenomenon. *See, e.g.*, Brown Shoe Co. v. United States, 370 U.S. 294 (1962).

[6] *See* 1984 VMGs (discussing the "Horizontal Effect from Non-Horizontal Mergers"); Jonathan B. Baker, Nancy L. Rose, Steven C. Salop & Fiona Scott Morton, *Five Principles for Vertical Merger Enforcement Policy*, 33 ANTITRUST 12, 13 (2019) ("[A]ll theories of harm from vertical mergers posit a horizontal interaction that is the ultimate source of harm").

- *Some acquisitions are ostensibly vertical in nature but nonetheless raise concerns on horizontal grounds. When the Agencies review such an acquisition, they will analyze the acquisition under the framework of the HMGs.* For example, a vertical merger may raise potential competition concerns when one or both of the merging parties had previously planned to enter the other's level of production before the merger. The Agencies will analyze this element of the merger as the combination of an actual and a potential competitor under the HMGs.

In connection with the last bullet point, we note that the Draft VMGs drop the more extended discussion of potential competition that appeared in the 1984 VMGs.[7] We worry that without an explicit mention of potential competition, this change in the VMGs, combined with the limited discussion of potential competition in the HMGs,[8] could be misinterpreted by some readers as indicating a retreat in Agency concern with this category of harm.[9] Additionally, some discussion of potential competition may be warranted to address distinctively vertical concerns—as, for example, when one of the merging parties is uniquely able to sponsor entry at the other's level of the supply chain.

SECTION 2. MARKET DEFINITION AND RELATED PRODUCTS

Clarify the Definition of the "Related Product" Concept

The Draft VMGs define the concept of a "related product" in Section 2:

> "A related product is a product or service that [1] is supplied by the merged firm, [2] is vertically related to the products and services in the relevant market, and [3] to which access by the merged firm's rivals affects competition in the relevant market."[10]

We recommend that the Agencies adopt the following alternative language for the third element of this definition: "to which access by the merged firm's rivals *could affect* competition in the relevant market." Without this change, the definition of the related product ostensibly depends on the conclusion of a competitive effects analysis.

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[7] 1984 VMGs, *supra* note 1, at § 4.1 ("Elimination of Specific Potential Entrants").

[8] While the HMGs expressly apply to mergers of potential competitors, HMGs, *supra* note 4, at § 1 ¶ 1 (identifying the scope of application as mergers "involving actual or *potential competitors*" (emphasis added)), they contain almost no specific discussion of potential competition concerns. *Cf. id.* at § 2.1.5 (the discussion of "the loss of actual or potential competition" resulting from the elimination of a maverick firm being the sole instance in which potential competition is specifically referenced in the HMGs outside of the introductory paragraph).

[9] *Cf.* Statement of Commissioner Rebecca Kelly Slaughter on the FTC-DOJ Draft Vertical Merger Guidelines Commission, File No. P810034, at 4 (Jan. 10, 2020), https://perma.cc/F4TW-3JYM (requesting greater emphasis of Agency investigation of potential competition concerns in the VMGs).

[10] Draft VMGs, *supra* note 2, at § 2 ¶ 2.

Consider Whether the "Related Product" Must Be Defined

The Draft VMGs appear to assert that the Agencies will *always* define a related product in the course of investigating a vertical theory of harm:

- Draft VMGs § 2: "When the Agencies identify a potential competitive concern in a relevant market, they *will* also specify one or more related products."[11]

- Draft VMGs § 3: appearing to imply that a related product will always be defined by incorporating it into the quasi-safe harbor provision.[12]

While we understand the potential usefulness of this concept as it relates to raising rivals' costs ("RRC") and foreclosure theories of harm, we are less confident about the potential usefulness—or, for that matter, relevance—of the related product concept as it relates to some other theories of harm, including concerns arising from access to competitively sensitive information.[13] We invite the Agencies to consider whether it would be more accurate and clarifying to preserve Agency discretion not to define a related product in appropriate circumstances.

SECTION 3. MARKET PARTICIPANTS, MARKET SHARES, AND MARKET CONCENTRATION

Consider Questions Not Addressed by the "Related Product" Concept

The Draft VMGs assert that "the share of the output in a relevant market that uses the related products" is a possible "measure[] of the competitive significance of the related product[]."[14] This is not a universally persuasive proposition.[15] Market definition provides an economic context in which output shares may be interpreted as measures of the relative competitive significance of products and firms *in the output relevant market*.[16] But the relationship between the output relevant market and its inputs is not always simple or straightforward.[17] The definition

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[11] *Id.* (emphasis added).
[12] *Id.* at § 3 ("The Agencies are unlikely to challenge a vertical merger where … the related product is used in less than 20 percent of the relevant market."). *But see id.* at § 3 ("The Agencies may *also* consider measures of the competitive significance of the related products as part of their evaluation of competitive effects in a relevant market.") (emphasis added) (suggesting that a "related product" may not need to be identified in all instances).
[13] *See id.* at § 5.b; *id.* at § 7 ¶ 3.
[14] *Id.* at § 3 ¶ 3.
[15] This is not to say that it is never persuasive. As an example, if the relevant market encompasses a homogenous good, if all producers utilize similar production technology, and if factor prices do not vary by location or producer, then an appropriate measure of the share of output attributable to a given input would seem to provide a reasonable estimate of that input's significance to competitors in the output relevant market. These conditions seem to be suggested by Example 2 in the Draft VMGs.
[16] *See generally* David Glasner & Sean P. Sullivan, *The Logic of Market Definition*, ANTITRUST L.J. (forthcoming).
[17] *See, e.g.,* Richard S. Higgins & William F. Shughart II, *Input Market Definition under Department of Justice Merger Guidelines*, 4 REV. INDUS. ORG. 99, 110 (1989) (noting that, among other things, "the substitution opportunities available to demanders in output markets constrain the power … [of] suppliers in input markets.").

of an output relevant market, without more, may not provide a sound basis for estimating the relative competitive significance of inputs.

We anticipate that the Agencies may encounter questions about how "the share of the relevant market that uses the related product" should be modified so as not to "understate [or overstate] the scope for material effects" in a given transaction.[18] By way of illustration, we raise the following questions, which are currently unaddressed in Sections 2 and 3 of the Draft VMGs.

- *How, if at all, would the availability of competitive sources of supply be accounted for in the share of the relevant market that uses the related product?* As a concrete example, if the related product is currently used in 30 percent of production, but half of this could be shifted to a substitute for the related product without any competitive impairment, would the related-product element of the quasi-safe harbor threshold still be satisfied?

- *How, if at all, would the unavailability of competitive sources of supply be accounted for in the share of the relevant market that uses the related product?* As a concrete example, if the related product is a critical input for a maverick firm with a 15 percent share of the output in the relevant market, would this situation still be one in which "[t]he Agencies are unlikely to challenge [the] merger?"[19]

- *How, if at all, would potential entry, repositioning, or expansion with respect to the supply of inputs be accounted for in the share of the relevant market that uses the related product?* As a concrete example, suppose that the share of the relevant market that uses the related product is 19% but could be expanded, that current suppliers of substitutes for the related product used in the relevant market are capacity constrained, and that other suppliers of substitutes for the related product currently do not supply any part of the relevant market. To what extent does the related product's 19% usage share of the output in the relevant market reflect its competitive significance? Note that, as the terms are used in the HMGs, market participants, rapid entrants, and entrants are defined only within the context of a relevant market.[20]

[18] *See id.* at § 3 ¶ 5 ("[T]he share of the relevant market that uses the related product may understate the scope for material effects if the related product is relatively new, and its share of use in the relevant market is rapidly growing.").
[19] *Id.* at § 3 ¶ 4. To the contrary, we anticipate that this would be an example of a situation in which "[a] merger[] with shares below the thresholds can give rise to competitive concerns." *Id.* at ¶ 4.
[20] *See* HMGs § 4 ¶ 1 ("market definition allows the Agencies to identify market participants and measure market shares and market concentration"); *id.* at § 5.1 (defining market participants and rapid entrants); *id.* at § 9 (describing entry analysis).

Preserve Flexibility in the Application of Quasi-Safe Harbors or Safety Zones[21]

To be candid, the 20% market-share and usage-share thresholds for the quasi-safe harbor provision seem arbitrary and unprincipled.[22] Whereas the Agencies have extensive experience working with the horizontal-merger concentration thresholds, and have indeed updated them over time,[23] the VMGs' quasi-safe harbor thresholds cannot—and do not—purport to command similar experience or authority. We read the Draft VMGs to recognize and address this lack of foundation with a relatively flexible quasi-safe harbor provision that leaves the Agencies discretion to pursue mergers that are identified as raising competitive concerns despite ostensibly low share figures.[24]

We believe this is a reasonable approach and recommend that the Agencies not undertake revisions to harden the quasi-safe harbor provision in this iteration of the VMGs. We anticipate that the accumulation of experience applying the new VMGs, and future developments in economic theory and empirical research, may lead the Agencies to revisit the quasi-safe harbor provision and thresholds in future revisions of the VMGs. This type of iterative approach would be wholly consistent with how the Agencies have revised and updated the HMGs over time.

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[21] We refer to the Draft VMGs' statement of enforcement likelihood, at the end of the second paragraph of section 3, as a "quasi-safe harbor," after Carl Shapiro's use of the same term in discussing the HMGs. *See* Carl Shapiro, *The 2010 Horizontal Merger Guidelines: From Hedgehog to Fox in Forty Years*, 77 ANTITRUST L.J. 701, 727 (2010). Alternatively, this statement could be called a "safety zone." *See* U.S. Dep't of Justice & Fed. Trade Comm'n, *Roundtable on Safe Harbours and Legal Presumptions in Competition Law – Note by the United States* § 1 ¶ 9 (Org. for Econ. Co-operation & Dev., Directorate for Fin. & Enter. Affairs, Dec. 5, 2017) [hereinafter "OECD Note"], https://perma.cc/5RSJ-PUBP (referring to the HMGs as including "'safety zones' that describe conditions under which the Agencies will not challenge conduct under the competition laws, absent extraordinary circumstances").

[22] Draft VMGs, *supra* note 2, at § 3 ¶¶ 4-5. *Cf.* Shapiro, *supra* note 21, at 727 & n.94 (touting the gross upward pricing pressure index (GUPPI) as being "well grounded in basic economics" and "far better grounded in basic economics than was the 35 percent [market share] presumption in the 1992 Guidelines"). Although RRC and foreclosure theories of harm are likewise "well grounded" in basic economics, we are unaware of any literature or decision specifying market-share and usage-share thresholds below which competitive harm would be unlikely. Indeed, a leading authority on RRC and foreclosure theories of harm has cautioned against taking such a "simple-minded" approach in analyzing vertical restraints. Steven C. Salop, *The Raising Rivals' Cost Foreclosure Paradigm, Conditional Pricing Practices, and the Flawed Incremental Price-Cost Test*, 81 ANTITRUST L.J. 371, 401 & n.126 (2017) ("This does not mean that courts should rely on simple-minded foreclosure rates…. A mechanical approach of measuring foreclosure simply by the fraction of customers or suppliers restrained by agreements can lead to error."). We urge the same caution in analyzing vertical mergers.

[23] *Compare* U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, 1997 MERGER GUIDELINES, §§ 1.5–1.51, https://perma.cc/6V3B-4N4G *with* HMGs, *supra* note 4, at § 5.3.

[24] *See* OECD Note, *supra* note 21, § 1 ¶ 9 ("Safety zones are similar to safe harbors but are not preclusive: conduct within a safety zone may still be challenged."); *see also id.* at § 4 ¶¶ 22–23 ("Conduct that falls within a safety zone is not exempt from the antitrust laws, nor does the existence of a safety zone preclude a finding of competitive infringement…. [I]f competitive conditions warrant, conduct falling within a safety zone can be legally challenged.").

SECTION 4. EVIDENCE OF ADVERSE COMPETITIVE EFFECTS

Relocate Discussion of Evidence of Adverse Competitive Effects

For logical clarity, we recommend that current Section 4 of the Draft VMGs be moved to precede current Section 2 ("Market Definition and Related Products"). This change helps to clarify the deeply empirical and fact-bound nature of inquiry in *all* sections of the VMGs. It also improves structural similarity between the HMGs and VMGs by positioning this discussion in the same location in each document, which will help readers as they are consulting both documents.[25]

SECTION 5. UNILATERAL EFFECTS

Eliminate Discussion of *De Minimis* Effects

The Draft VMGs briefly reference a requirement of effects "[t]he magnitude [of which] is not *de minimis* such that it would substantially lessen competition."[26] We are uncertain what the Agencies mean to achieve with this language. The term "*de minimis*" is never used in the HMGs.[27] Indeed, as far as we are aware, no U.S. merger guidelines have ever used the term to qualify the scope of effects, or magnitude of injury, that warrants Agency scrutiny and potential challenge under Section 7. Below, we address several potential interpretations of this language. In every case—and especially given the inherent ambiguity in this language—we recommend that the Agencies eliminate the discussion of "*de minimis*" effects from the VMGs.

If the point of this language is simply to recognize that the extent of foreclosure is relevant to a showing of harm under Section 7 of the Clayton Act, then a precise way to express this sentiment is in terms of the statutory standard: "the magnitude of likely foreclosure or raising rivals' costs is such that it may be substantially to lessen competition."[28] This wording has the advantage of focusing attention on the ultimate question under Section 7—whether the effect of the merger may be substantially to lessen competition in any relevant market.[29]

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[25] *See* HMGs, *supra* note 4, at § 2 ("Evidence of Adverse Competitive Effects").
[26] Draft VMGs, *supra* note 2, at § 5.a.
[27] *See generally* HMGs, *supra* note 4.
[28] *See* Clayton Act, ch. 323, § 7, 38 Stat. 730, 731-32 (1914) (current version at 15 U.S.C. § 18 (2018)) (prohibiting mergers, the effects of which "may be substantially to lessen competition, or to tend to create a monopoly").
[29] This is consistent with the approach taken by the Supreme Court: treating *de minimis* foreclosure as of secondary and derivative interest to the controlling question whether a merger tends substantially to lessen competition. *See* Brown Shoe Co. v. United States, 370 U.S. 294, 329 (1962) ("On the other hand, foreclosure of a *de minimis* share of the market will not tend 'substantially to lessen competition.' Between these extremes, in cases such as the one before us, in which the foreclosure is neither of monopoly nor *de minimis* proportions, the percentage of the market foreclosed by the vertical arrangement cannot itself be decisive.").

If the point of this language is to suggest a quantitative definition of *de minimis* harm,[30] then we ask that the Agencies reconsider this strategy. At a minimum, this appears to presuppose that harm to competition can always be quantified. But precise quantification is often impossible—for example, in coordinated effects cases.[31] Moreover, "substantiality" under the Clayton Act may have multiple dimensions—*e.g.,* level of price increase, number of consumers impacted, key innovation shutdown. It may also depend upon such fact-intensive considerations such as the history of competition or of acquisitions within an industry or sector.[32] Attempted quantification of the substantiality threshold also stands in possible tension with judicial interpretations of the Clayton Act that have declined to read any specific quantitative threshold into the statute.[33]

Finally, if the point of this language is to suggest a quantitative definition of *de minimis* harm as an expression of prosecutorial discretion,[34] then we observe that deep policy considerations can and should attach to the identification of something like a threshold quantity of injury below which the Agencies will not investigate mergers or seek to enforce the Clayton Act. While the Agencies have wide prosecutorial discretion, we question the wisdom of committing to any specific exercise of that discretion in this document—particularly when the underlying motivations for a given policy decision are susceptible to change as government viewpoints, economic learning, and Agency experience continue to evolve.

Resolve Inconsistent Assertions of Enforcement Likelihood

The Draft VMGs' discussion of foreclosure and RRC theories includes subtle differences in the statement of how likely the Agencies are to investigate and challenge a merger:

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[30] *See* Concurring Statement of Christine S. Wilson on the Publication of FTC-DOJ Draft Vertical Merger Guidelines for Public Comment, File No. P810034 (January 10, 2020), https://perma.cc/VPN2-GASU ("What magnitude of anticompetitive effects should we view as *de minimis*, in light of EDM and likely vertical efficiencies?").
[31] *See* HMGs, *supra* note 4, at § 7.1 ("There are, however, numerous forms of coordination, and the risk that a merger will induce adverse coordinated effects may not be susceptible to quantification or detailed proof.").
[32] This broad scope of analysis is among the oldest and most enduring propositions in antitrust law. *See, e.g.*, United States v. Philadelphia Nat. Bank, 374 U.S. 321, 367 (1963) (assessing a merger "in view of the strong trend toward [concentration-increasing] mergers evident in the area"); *Brown Shoe*, 370 U.S. at 344–45 ("[F]actors to be considered in evaluating the probable effects of a merger [include] … the history of tendency toward concentration in the industry."); Bd. of Trade of City of Chicago v. United States, 246 U.S. 231, 238 (1918) (including in the ordinary scope of rule of reason analysis "the facts peculiar to the business ... its condition before and after the restraint was imposed; the nature of the restraint and its effect, actual or probable. The history of the restraint, the evil believed to exist, the reason for adopting the particular remedy, the purpose or end sought to be attained ...").
[33] *See Brown Shoe*, 370 U.S. at 320–21 ("Congress … did [not] adopt a definition of the word 'substantially,' whether in quantitative terms of sales or assets or market shares or in designated qualitative terms, by which a merger's effects on competition were to be measured."); *id.* at 321–22 ("[W]hile providing no definite quantitative or qualitative tests by which enforcement agencies could gauge the effects of a given merger to determine whether it may 'substantially' lessen competition or tend toward monopoly, Congress indicated plainly that a merger had to be functionally viewed, in the context of its particular industry."); Sprint Nextel Corp. v. AT&T, Inc., 821 F. Supp. 2d 308, 333 (D.D.C. 2011) ("Defendants have cited no case establishing a *de minimis* exception to antitrust injury. Even if Corr Wireless represents only a small part of Cellular South's business, Cellular South's allegations suggest that its threatened loss from the merger is plausible.").
[34] *See supra* note 30.

- "potentially raise[s] significant competitive concerns *and often warrant[s] scrutiny*"[35]

- "potentially raises significant competitive concerns *and may warrant scrutiny*"[36]

It is unclear whether this difference in wording is intended to suggest a difference in enforcement conviction between the two contexts (enumeration of conditions under which foreclosure or RRC can harm competition vs. illustrative hypothetical examples).[37] If this *is* intended, clarity may be improved by identifying the motivating differences; if not, clarity may be improved by adopting parallel language or by parenthetical explanation that no difference in enforcement conviction is intended.

Reconsider Weak Assertions of Enforcement Likelihood

The Draft VMGs discuss hypothetical merger investigations in which the investigating agency reaches the following conclusions:[38]

1. RRC would be effective against rivals
2. The effect of RRC would be to the benefit of the merged firm
3. The RRC incentive would not exist without the merger[39]
4. The magnitude of predicted effects is not de minimis

Yet the Draft VMGs claim only that mergers like these "*potentially* raise significant competitive concerns and *often* warrant scrutiny."[40] While we recognize the importance of caution when conveying the anticompetitive potential of hypothetical mergers devoid of factual context, we suggest that the Agencies consider whether this statement of enforcement likelihood may depart from or contradict the statutory standard. We suggest the following language instead: "raises significant competitive concerns, thereby warranting scrutiny." This language does not commit that the Agencies will bring a challenge; it simply identifies this type of merger as presenting the kind of potential harm that warrants Agency investigation.

[35] Draft VMGs, *supra* note 2, at § 5.a ¶ 4.
[36] *E.g.*, *id.* at Example 3.
[37] *Compare id.* at § 5.a ¶ 4 *with id.* at Examples 3, 5 and 6.
[38] *Id.* at 5.
[39] We are uncertain why this is element is required. An *increase* in the incentive to engage in anticompetitive conduct would seem sufficient to meet the statutory standard. This is the paradigm adopted by the HMGs. *See, e.g.*, HMGs, *supra* note 4, at § 1 ¶ 7 ("*Enhancement* of market power by sellers often *elevates* the prices charged to customers.") (emphasis added); *id.* at § 7.1 ¶ 1 ("The Agencies examine whether a merger is likely to change the manner in which market participants interact, inducing substantially *more* coordinated interaction." (emphasis added)).
[40] Draft VMGs, *supra* note 2, at 5 (emphasis added); *cf.* HMGs, *supra* note 4, at § 5.3 (only using the same language, "potentially raise significant competitive concerns and often warrant scrutiny," in the less developed context of mergers producing moderately or highly concentrated markets by sufficient increases in market concentration).

Relocate Discussion of EDM

We understand the Draft VMGs to position discussion of EDM immediately after discussion of unilateral effects as a way of emphasizing the intrinsic relationship between RRC theories and the pricing implications of EDM. While this relationship is indeed important, we are concerned that organizing the material in this way may do more harm than good. Our concerns divide into roughly three categories.

First, we are concerned that separating EDM from efficiencies analysis is likely to confuse some courts and lay readers. We recognize the theoretical arguments for treating EDM differently from other cognizable efficiencies within RRC analysis but note that (1) not all unilateral effects arise from RRC models, and (2) not all considerations of EDM relate to RRC.[41] While expert readers will understand and recognize that arguments for the special treatment of EDM in RRC models do not translate to all other competitive effect concerns,[42] we are concerned that lay readers of the VMGs could be misled by this treatment of EDM outside of the RRC context.

With lay readers in mind, we suggest that the Agencies consider how the effects of EDM in vertical merger analysis will often be similar to marginal cost efficiencies in horizontal effects applications. Indeed, there is an intuitive analogy between the effect of EDM in RRC models and the effect of marginal cost efficiencies in standard (horizontal) unilateral-effects models.[43] The argument for grouping EDM with other efficiencies is especially strong when one considers that both influences will need to be accounted for in net price analysis. Apples are not precisely the same as oranges, but it is no coincidence that both are typically found in the fruit section. We suggest that EDM be placed under the heading of merger efficiencies.

Second, we are concerned that separating EDM from the analysis of other efficiencies may be exploited to allow for a less searching analysis of EDM than is typically expected of other merger efficiencies. Without a strong empirical basis to justify it, we believe it would be a mistake to subject EDM to anything less than the following practices and requirements:

- To be credited in competitive effects analysis EDM should be "cognizable" within the definition of the HMGs.[44] This requires application of the rubric of merger specificity.

[41] As just one example, the Draft VMGs return to the topic of EDM in the discussion of coordinated effects. Draft VMGs, *supra* note 2, at 8.

[42] *See* Baker et al., *supra* note 6 at 13 (discussing various ways that vertical mergers may harm competition); Gopal Das Varma & Martino De Stefano, *Equilibrium Analysis of Vertical Mergers*, at 20 (Dec. 10, 2018), https://ssrn.com/abstract=3307150 ("Even if a vertical merger does not raise rivals' cost, it might still need to be scrutinized for other potential anti-competitive effects.").

[43] *Compare* Draft VMGs, *supra* note 2, at § 6 ¶ 1 ("[C]apturing the upstream margin, through merger, may make the price reduction profitable even though it would not have been profitable prior to the merger") *with* HMGs, *supra* note 4, at § 10 ¶ 1 ("In a unilateral effects context, incremental cost reductions may reduce or reverse any increases in the merged firm's incentive to elevate price.").

[44] HMGs, *supra* note 4, at § 10 ¶ 5.

- The influence of EDM should be assessed as an empirical question bound by the evidence, not a theoretical supposition to be accepted unless specifically disproven.[45]

- In general, the burden of proving the effects of EDM should be on the merging parties, who presumably can best and at least cost produce evidence of this effect. Where the Agencies assert that they have duly accounted for EDM as part of an RRC model of harm, however, they would bear the same burden on this proposition that they do on all other propositions asserted in proving their case in chief.

Broadly, we are concerned that the separate treatment of EDM could be read by non-experts as implying that EDM is a standard byproduct of vertical mergers when in fact its existence and full realization are inherently fact-bound and dependent on characteristics of the merging parties and the premerger relationship between their respective upstream and downstream businesses.[46]

Third, from a logical perspective, it makes little sense to sandwich the two competitive effects sections around a topic that is—in many respects—closer to a defense on the merits. Compare the striking parallels in discussion of EDM in the Draft VMGs and efficiencies in the HMGs:

- Draft VMGs § 6 (EDM): "The Agencies will not challenge a merger if the net effect of elimination of double marginalization means that the merger is unlikely to be anticompetitive in any relevant market."[47]

- HMGs § 10 (Efficiencies): "The Agencies will not challenge a merger if cognizable efficiencies are of a character and magnitude such that the merger is not likely to be anticompetitive in any relevant market."[48]

Clarity and accuracy will be improved by accompanying this parallel language with a parallel positioning of EDM within the discussion of efficiencies in the Draft VMGs. Additionally, the VMGs' discussion of competitive effects will then mirror the consecutive treatment of unilateral and coordinated effects in the HMGs,[49] thereby helping readers better navigate these documents.

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[45] For example, in the case of multiproduct firms, the realization of EDM for some products makes them cheaper, and hence relatively more profitable to sell. That in turn may incentivize the merged firm to raise the prices of other products that are not subject to EDM, so as to divert those sales to the products that are subject to EDM. This is known as the Edgeworth-Salinger effect, and its presence can result in price increases, EDM notwithstanding. *See* Fernando Luco & Guillermo Marshall, *Vertical Integration with Multiproduct Firms: When Eliminating Double Marginalization May Hurt Consumers* 2 (Dec. 7, 2018) (measuring the countervailing effects of EDM and Edgeworth-Salinger post-acquisition in mergers between upstream firms like Coca-Cola and Pepsi that manufacture concentrate and downstream bottlers that mix the concentrate with carbonated water to produce branded sodas), https://ssrn.com/abstract=3110038.

[46] *See, e.g.,* Fred M. Westfield, *Vertical Integration: Does Product Price Rise or Fall?*, 71 AM. ECON. REV. 334, 336 (1981) ("Although vertical merger may lead to product price decrease when a nonzero elasticity of substitution at the benchmark price is low, a sufficiently high price elasticity of product demand for integrated monopoly, producing given equilibrium output, will always outweigh this effect of low substitution elasticity.").

[47] Draft VMGs, *supra* note 2, at § 6 ¶ 3.

[48] HMGs, *supra* note 4, at § 10 ¶ 6.

[49] *Id.* at §§ 6–7.

SECTION 7. COORDINATED EFFECTS

Clarify Distinctions between Vertical and Horizontal Coordinated Effects Analysis

We believe that some readers would benefit from a discussion of how market structure factors into coordination theories in the vertical context. This discussion need not be extensive, but it may be important to alert non-expert readers to the Agencies' discretion to analyze coordination concerns outside of the framework of the HMGs.[50] The Draft VMGs already contemplate this possibility: "The theories of harm discussed in the Horizontal Merger Guidelines, as well as those discussed below, are not exhaustive, but rather are illustrations of the manner in which a merger may lessen competition due to coordinated effects."[51] We propose the Agencies go one step further by observing that changes in market concentration are not necessary in a coordination theory of harm.[52] The following example illustrates this point:

> *Example.* Suppose that firms A, B, and C have a failed history of attempting to coordinate their pricing, due in part to C's lack of vertical integration. C is now proposing to vertically integrate through acquisition. The merger produces no HHI delta in any relevant market, and thus fails to fit the HMGs' analysis of coordination.[53] The Agencies would instead analyze the merger's potential for facilitating coordination under the framework of the VMGs.[54]

We note that the Draft VMGs come very close to making this exact point in Section 3: "The Agencies … do not rely on changes in concentration as a screen for or indicator of competitive effects from vertical theories of harm."[55] We believe, however, that clarity would be improved by reiterating this statement, or by providing an illustrative example, in the coordination context.

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[50] *See id.* at § 7.
[51] Draft VMGs, *supra* note 2, at § 7 ¶ 1.
[52] *See* HMGs, *supra* note 4, at § 7.1 (requiring the merger to "significantly increase concentration" and limiting the scope of vulnerability assessment "to moderately and highly concentrated markets").
[53] *Cf. id.* at § 7.1 ¶ 2 ("The Agencies are likely to challenge a merger if the following three conditions are all met: (1) the merger would significantly increase concentration and lead to a moderately or highly concentrated market…").
[54] A possible theory under the VMGs is that the vertical merger creates greater multimarket interdependence among firms A, B, and C. *See* Yongmin Chen, *On Vertical Mergers and Their Competitive Effects*, 32 RAND J. ECON. 667, 681 (2001). Another theory is that the merger may reduce or eliminate the incentives of previously unintegrated firms to resist certain types of coordinated conduct. *See* Draft VMGs, *supra* note 2, at § 7 ¶ 2 (discussing "maverick" firms); Volker Nocke & Lucy White, *Do Vertical Mergers Facilitate Upstream Collusion*, 97 AM. ECON REV. 1321, 1322 (2007) (describing the "outlets effect" of vertical mergers, i.e., reducing the number of outlets through which rivals of the upstream merging firm can sell when deviating from a collusive agreement, thereby reducing their profit from cheating).
[55] Draft VMGs, *supra* note 2, at § 3 ¶ 2.