Expect Merger Enforcement To Roll Full Steam Ahead

By **Christopher Williams, Caroline Gizem Tunca and Tiffany Lee** (April 7, 2023)

Christopher Williams

Caroline Gizem Tunca

Tiffany Lee

At the American Bar Association's 2023 Antitrust Spring Meeting, held in March in Washington, D.C., representatives of the U.S. Department of Justice's Antitrust Division and Federal Trade Commission confirmed their agenda to reinvigorate and modernize antitrust merger enforcement.

Federal enforcers conveyed a consistent theme that the past four decades of antitrust enforcement have been plagued by fear of overenforcement and by overreliance on rigid economic models that fail to capture market realities.

The antitrust agencies have not been afraid to bring more difficult merger challenges, but they have had limited success in litigation. However, DOJ and FTC representatives projected confidence and optimism despite recent setbacks in court.

The DOJ has lost three of its last four merger challenges in federal court. Two challenges — U.S. v. U.S. Sugar Corp. in the U.S. District Court for the District of Delaware on Sept. 23 and U.S. v. Booz Allen Hamilton Holdings Corp. in the U.S. District Court for the District of Maryland on Oct. 11 — failed because the court found that the DOJ did not carry its burden to define a relevant antitrust market under the Clayton Act.

The third loss, in U.S. v. United Health Group Inc. in the U.S. District Court for the District of Columbia on Sept. 19, involved both horizontal and vertical theories of harm. There, the court accepted the parties' "fix-it-first" remedy and rejected the DOJ's vertical theory of harm.

After these three losses, the DOJ finally got a win on Oct. 31, obtaining a permanent injunction of Penguin Random House's proposed acquisition of Simon & Schuster. This was a monopoly case where U.S. District Judge Florence Pan in D.C. federal court sided with the DOJ's argument that the acquisition would have been likely to "result in substantial harm to authors of anticipated top-selling books and ultimately, consumers."[1]

On Jan. 31, the FTC failed to enjoin Meta's acquisition of Within in FTC v. Meta Platforms Inc. in the U.S. District Court for the Northern District of California. While the court acknowledged the FTC's potential competition theories of harm, it found that the agency did not show it was reasonably probable that Meta would enter the market de novo or was perceived as a potential de novo entrant.

The FTC also lost two administrative complaints before its own administrative law judge: the first on Feb. 23, 2022, involving Altria's acquisition of a 35% interest in JUUL, and the second on Sept. 1 involving its vertical challenge of Illumina's acquisition of Grail.

But the DOJ and FTC seem undeterred by their recent losses. At the "Enforcers Roundtable" and "DOJ Update" sessions, agency leadership touted that their aggressive merger enforcement strategy has largely been successful at deterring anti-competitive mergers

despite these losses, in stark contrast to the overenforcement concerns that have motivated the agenda of prior administrations.

In sum, the DOJ and FTC will continue to bring challenging cases they believe may harm competition, signaling that hot-button issues like nonhorizontal mergers, potential competition, acquisitions in nascent markets, serial acquisitions, private equity acquisitions and mergers involving buy-side issues, such as labor markets, may be addressed in the new draft merger guidelines, which FTC Chair Lina Khan said should be shared "in short order."

What does this mean for merging parties and their counsel?

Be Prepared to Litigate, Especially Against the DOJ

Assistant Attorney General Jonathan Kanter expressed at the "Enforcers Roundtable" that litigation is a far more effective tool for protecting competition than divestiture and other remedies. This suggests that the DOJ will more likely pursue litigation rather than structural remedies and that conduct remedies, which have been historically common in nonhorizontal mergers, are almost certainly off the table.

While the DOJ has not reached any merger consents under Kanter's leadership, Deputy Assistant Attorney General Andrew Forman said at the "DOJ Update" session that divestitures by consent decree are not off limits. However, he reiterated that there is "an extremely high bar."

Another reason the DOJ is more willing to pursue litigation is that the administration wants to take risks to "move the law forward" and "ask the courts to reconsider the application of old precedents to [modern] markets."[2]

Kanter contended that concepts of horizontal and vertical relationships do not fit modern market realities, arguing that showing direct evidence of anti-competitive harm may better reflect anti-competitive effects than indirect evidence of market power through artificially constructed markets and market shares. We expect significant discussion in this area in the upcoming draft merger guidelines.

Finally, the DOJ recognized the deterrent value of vigorous regulation and litigation. Specifically, Kanter highlighted that there are "many more" abandonments of mergers that are not public.

While the FTC has been more willing to agree to consent remedies, it has not been shy at seeking to block mergers.

On April 3, the FTC reversed the administrative law judge's decision to dismiss the FTC's administrative complaint challenging Illumina's acquisition of Grail, requiring Illumina to divest Grail.

Also, several transactions have been abandoned following threatened or filed FTC suits.

Remedies With the FTC Will Come at a Cost

At the "Private Equity: Villain or Bogeyman" session, Deputy Director Rahul Rao of the FTC's Bureau of Competition discussed the agency's reinvigorated enforcement efforts, including regular use of prior notice and approval requirements in merger settlements.

On Oct. 25, 2021, the FTC issued a policy statement reinstating its prior notice and approval practice for parties subject to an FTC order for a minimum of 10 years. Since then, the agency has regularly included requirements in its divestiture orders for merging parties to obtain approval for any acquisitions involving the relevant markets for a 10-year period.

With limited exceptions, the commission has required divestiture buyers to obtain prior approval to sell the divested assets for a three-year period, with an additional seven-year period during which the divestiture buyer must obtain prior approval before selling to a competitor in the same relevant product and geographic market as the divested asset.

The FTC has also tried to impose prior approval requirements following the administrative law judge's dismissal of its administrative complaints related to Illumina's acquisition of Grail and Altria's investment in JUUL.

In Illumina-Grail, the FTC prohibited Illumina from acquiring without prior approval for 10 years any ownership in Grail or any other business that engaged or had plans to engage in the development, marketing or sale of multicancer early detection tests. On March 31, the FTC ordered Illumina to divest the $7.1 billion acquisition of Grail, a sign that the FTC's strong stance toward deal-making continues.

In Altria-JUUL, Altria unwound its 35% stake in JUUL and sought dismissal of the appeal to the FTC as moot. The FTC, however, denied the stay and is considering imposing prior approval restrictions on any transactions between Altria and JUUL or any third party in the relevant e-cigarette market.

The lesson: The more resources the FTC expends investigating or litigating a transaction, the more likely it will seek prior approval requirements to avoid relitigating a similar transaction in the future involving those parties.

The Agencies Will Bring More Future Competition and Nonhorizontal Merger Cases

Despite recent setbacks in potential competition and nonhorizontal merger cases, enforcers still projected confidence in their enforcement agenda.

Both agencies appear keen to pursue test cases and stretch the law in this area, particularly in technology and digital markets.

These theories of harm will be addressed in the draft merger guidelines, possibly with lower market concentration presumptions — if they are retained at all — and more emphasis on challenging mergers using evidence of direct effects.

Notably, even in defeat, Khan, at the "Enforcers Roundtable" session, called the Meta-Within decision "an important programmatic win" for the FTC because the court accepted the legal theory of harm to actual and prospective potential competition and provided a "road map" for future enforcement of mergers involving nascent markets and potential competitors.

Expect Increased Enforcement of Industry Roll-Ups and Serial Acquisitions

At the "Private Equity: Villain or Bogeyman" session, Rao and Catherine Reilly, DOJ counsel for civil operations, discussed how the agencies are paying close attention to roll-up strategies where a buyer, often a private equity firm, consolidates the market via a series of acquisitions of competitors.

Usually, these serial acquisitions are small and fall under the Hart-Scott-Rodino Act's reportability thresholds. However, the agencies have the authority to challenge nonreportable transactions even after they are consummated.

The agencies are exploring ways to better monitor and enforce potentially anti-competitive roll-ups, including under monopolization theories of harm under Section 2 of the Sherman Act in addition to Section 7 of the Clayton Act, which prohibits mergers where the effect "may be substantially to lessen competition, or to tend to create a monopoly."[3]

Kanter stressed that the second prong — "tend to create a monopoly" — has been ignored over the years and will be a part of the DOJ's future challenges, particularly those involving serial acquisitions.

One of the FTC's tools to catch future roll-ups is requiring prior notice and approval of future transactions — of any size in the relevant market — in its consent orders.

Increased Scrutiny of Private Equity Acquisitions

Also at the "Private Equity: Villain or Bogeyman" session, DOJ and FTC representatives expressed concerns over private equity acquisitions, particularly in health care.

The panelists discussed studies suggesting a correlation between private equity ownership of health care facilities with higher prices, lower wages, degraded quality of care and, in the context of nursing homes, increased deaths.

The concern is that private equity acquisitions are often heavily leveraged with debt that incentivizes short-term profits and cost-cutting measures at the expense of the business's long-term health and ability to compete — i.e., the strip-and-flip model.

However, the agencies recognize that not all private equity buyers are heavily leveraged or follow a strip-and-flip strategy, and generally apply the same rules to private equity as other transactions.

Nevertheless, private equity companies should be mindful that the agencies are watching this space, particularly industry roll-ups.

DOJ Is Serious About Unwinding Interlocking Directorates

Kanter, at the "Enforcers Roundtable," highlighted the DOJ's increased efforts to enforce the prohibition on interlocking directorates in Section 8 of the Clayton Act, which he claimed has never seen "systematic" enforcement "until now."

He noted that roughly 15 directors have stepped down from boards of competing companies in response to DOJ inquiries into interlocks and that there are roughly 20 open investigations into additional Section 8 violations.

Several interlocks involved representatives from private equity companies. The DOJ has adopted the deputization theory, which — while not settled by the courts — finds an interlock where an entity, such as a private equity firm, has appointed agents or representatives to the boards of competing companies, even where such representatives are different people.

Expect HSR Enforcement Actions on Gun-Jumping and Missed Item 4 Documents

At the "DOJ Update" session, Forman stated that the agencies are dedicating more resources toward ensuring compliance with the HSR Act, noting that there are open investigations into violations of the act for failing to file Item 4(c) and Item 4(d) documents, as well as for gun-jumping.

The maximum civil penalty for violations of the act is $50,120 per day in violation. Parties should take their filing obligations seriously and ensure that they have appropriate measures in place regarding the exchange of information, integration planning and other preclosing activities.

Practical Takeaways

In sum, despite significant setbacks in court, the Biden administration's antitrust enforcers are pushing ahead with their robust enforcement agenda.

Parties to a transaction that may present competition issues, including ones that may have nuanced issues in nonhorizontal markets, should be ready for the agencies to heavily scrutinize their deal and be prepared to litigate.

Christopher A. Williams is a partner, Caroline Gizem Tunca is an associate and Tiffany Lee is counsel at Perkins Coie LLP.

[1] DOJ Complaint at 4, U.S. v. Bertelsmann SE & Co. KGaA, https://www.justice.gov/atr/case-document/file/1445931/download.

[2] Assistant Attorney General Jonathan Kanter of the Antitrust Division Delivers Remarks to the New York State Bar Association Antitrust Section (Jan. 24, 2022), https://www.justice.gov/opa/speech/assistant-attorney-general-jonathan-kanter-antitrust-division-delivers-remarks-new-york.

[3] 15 U.S.C. § 18.