ROUNDTABLE ON SUBSTANTIVE CRITERIA USED FOR MERGER ASSESSMENT

Note by the United States

1. The United States uses a "substantial lessening of competition" test for merger analysis. Mergers are prohibited if their effect may be "substantially to lessen competition, or to tend to create a monopoly " "in any line of commerce… in any section of the country." Clayton Act §7, 15 U.S.C. § 18. Mergers may also be challenged under the Sherman Act, 15 U.S.C. § 1 or the Federal Trade Commission Act, 15 U.S.C. §

2. Competitive Effects of a Merger

5. In the United States, the agencies take an economically driven, consumer welfare approach to merger review whereby the agencies evaluate the likely net effect of a transaction on price and output. The analytical approach to merger review recognises consumer benefits by pursuing merger enforcement only against mergers likely to be harmful, while otherwise relying on market forces to operate (including through lawful mergers) to benefit consumers.

6. While challenging competitively harmful mergers, the agencies seek to avoid unnecessary interference with the larger universe of mergers that are either competitively beneficial or neutral. In implementing this objective, however, the Guidelines reflect the congressional intent that merger enforcement should interdict competitive problems in their incipiency.

7. The agencies assess whether the merger, in light of market concentration and other factors that characterise the market, raises concern about potential adverse competitive effects. A merger may diminish competition by enabling the firms selling in the relevant market more likely, more successfully, or more completely to engage in co-ordinated interaction that harms consumers. Lessening of competition through co-ordinated interaction is discussed in section 2.1 of the Guidelines and below. A merger may diminish competition even if it does not lead to increase likelihood of successful co-ordinated interaction, because merging firms may find it profitable to alter their behaviour unilaterally following the merger by elevating price and suppressing output. Lessening of competition through unilateral effects is discussed in section 2.2 of the Guidelines and below.

3. Efficiencies

8. First, the law takes account of efficiency gains by employing a standard under which mergers do not need formal approval of the government -- rather; all mergers are lawful unless they violate the statute. Thus, "[w]hile challenging competitively harmful mergers, the Agenc[ies] seek[] to avoid unnecessary interference with the larger universe of mergers that are either competitively beneficial or neutral." GUIDELINES 0.1

9. Second, as the Guidelines describe, the agencies undertake a specific analysis of efficiency issues. In 1997, the Department of justice and the Federal Trade Commission revised a portion of their joint Horizontal Merger Guidelines to clarify how the agencies analyse claims that a merger is likely to lower costs, improve product quality, or otherwise achieve efficiencies. The revisions make clear that the agencies will take efficiencies into account as part of their analysis of the competitive effects of the merger. The revisions also provide explicit guidance on issues such as: how the agencies determine if the claimed efficiencies are properly attributable to the merger; what the parties must do to substantiate their efficiencies claims; the circumstances, as a practical matter, in which the agencies are likely to find efficiencies claims persuasive; and the circumstances under which consideration will be given to out-of-market efficiencies and to in-market efficiencies that are not expected to have short-term, direct effects on prices. Efficiencies are discussed in section 4 of the Guidelines and below.

4. Failing firms

10. The agencies assess whether, but for the merger, either party to the transaction would be likely to fail, causing its assets to exit the market. The theory is that "[a] merger is not likely to create or enhance market power or to facilitate its exercise, if imminent failure of one of the merging firms would cause the assets of that firm to exit the relevant market. In such circumstances, post-merger performance in the

relevant market may be no worse than market performance had the merger been blocked and the assets left the market." GUIDELINES 5.0 *See below* for a description of the analytical steps in applying this principle.

5. Application of the Substantive Standard

a violation of the Clayton Act is established, the goal is not to review the market and decide how it would best operate or to resolve problems that were not caused by the transaction. Instead, the goal is to remedy

offered lower prices, they would report that to the buying group who got the outlaw to bring prices back to the agreed upon pricing matrix. Because of these agreements, the court believed that three of the four defendants engaged in a "subtle form of price stabilisation" that could assist the merging firms to tacitly collude.

2. Entry impediments: The court stated that "[a] court's finding that there exists ease of entry into the relevant product market can be sufficient to offset the government

1. First, the agencies assess whether the merger would significantly increase concentration and result in a concentrated market, properly defined and measured.

2. Second, the agencies assess whether the merger, in light of market concentration and other factors that characterise the market, raises concern about potential adverse competitive effects.

3. Third, the agencies assess whether entry would be timely, likely and sufficient either to deter or to counteract the competitive effects of concern.

4. Fourth, the agencies assess any efficiency gains that reasonably cannot be achieved by the parties through other means.

5. Finally, the agencies assess whether, but for the merger, either party to the transaction would be likely to fail, causing its assets to exit the market.

7.1 Definition of Markets and Assessment of Concentration

> "First, the agencies assess whether the merger would significantly increase concentration and result in a concentrated market, properly defined and measured."

21. A merger is unlikely to create or enhance market power or to facilitate its exercise unless it significantly increases concentration and results in a concentrated market, properly defined and measured. Mergers that either do not significantly increase concentration or do not result in a concentrated market ordinarily require no further analysis.

22. The analytic process described here ensures that the agencies evaluate the likely competitive impact of a merger within the context of economically meaningful markets - - *i.e.*, markets that could be subject to the exercise of market power. Accordingly, for each product or service (hereafter "product") of each merging firm, the agencies seek to define a market in which firms could effectively exercise market power if they were able to co-ordinate their actions.

23. Market definition focuses solely on demand substitution factors -- *i.e.*, possible consumer responses. Supply substitution factors -- *i.e.*

provide a useful framework for merger analysis, the numerical divisions suggest greater precision than is possible with the available economic tools and information. In addition, as discussed below, market share concentration is only the starting point for analysis -- concentration in and of itself is insufficient to justify an enforcement action.

26. General Standards. In evaluating horizontal mergers, the agencies consider both the post-merger market concentration and the increase in concentration resulting from the merger. Market concentration is a useful indicator of the likely potential competitive effect of a merger. The general standards for horizontal mergers are as follows:

a) Post-Merger HHI Below 1000. The agencies regard markets in this region to be unconcentrated. Mergers resulting in unconcentrated markets are unlikely to have adverse competitive effects and ordinarily require no further analysis.

b) Post-Merger HHI Between 1000 and 1800. The agencies regard markets in this region to be moderately concentrated. Mergers producing an increase in the HHI of less than 100 points in moderately concentrated markets post-merger are unlikely to have adverse competitive consequences and ordinarily require no further analysis. Mergers producing an increase in the HHI of more than 100 points in moderately concentrated markets post-merger potentially raise significant competitive concerns depending on the factors set forth in the competitive effects analysis of the Guidelines.

c) Post-Merger HHI Above 1800. The agencies regard markets in this region to be highly concentrated. Mergers producing an increase in the HHI of less than 50 points, even in highly concentrated markets post-merger, are unlikely to have adverse competitive consequences and ordinarily require no further analysis. Mergers producing an increase in the HHI of more than 50 points in highly concentrated markets post-merger potentially raise significant competitive concerns, depending on the factors set forth in the competitive effects analysis of the Guidelines. Where the post-merger HHI exceeds 1800, it will be presumed that mergers producing an increase in the HHI of more than 100 points are likely to create or enhance market power or facilitate its exercise. The presumption may be overcome by a showing that factors set forth in the competitive effects analysis of the Guidelines make it unlikely that the merger will create or enhance market power or facilitate

(b) Degree of Difference between the Products and Locations in the Market and Substitutes outside the Market. All else equals, the magnitude of potential competitive harm from a merger is greater if a hypothetical monopolist would raise price within the relevant market by substantially more than a "small but significant and nontransitory" amount. This may occur when the demand substitutes outside the relevant market, as a group, are not close substitutes for the products and locations within the relevant market. There thus may be a wide gap in the chain of demand substitutes at the edge of the product and geographic market. Under such circumstances, more market power is at stake in the relevant market than in a market in which a hypothetical monopolist would raise price by exactly five percent.

7.2 Evaluation of Potential Adverse Competitive Effects

"Second, the agencies assess whether the merger, in light of market concentration and other factors that characterise the market, raises concern about potential adverse competitive effects."

28. Other things being equal, market concentration affects the likelihood that one firm, or a small group of firms, could successfully exercise market power. The smaller the percentage of total supply that a firm controls, the more severely it must restrict its own output in order to produce a given price increase, and the less likely it is that an output restriction will be profitable. If collective action is necessary for the exercise of market power, as the number of firms necessary to control a given percentage of total supply decreases, the difficulties and costs of reaching and enforcing an understanding with respect to the control of that supply might be reduced. However, market share and concentration data provide only the starting point for analysing the competitive impact of a merger. Before determining whether to challenge a merger, the agencies also will assess the other market factors that pertain to competitive effects, as well as entry, efficiencies and failure.

7.2.1 Lessening of Competition through Co-ordinated Interaction

29. A merger may diminish competition by enabling the firms selling in the relevant market more likely, more successfully, or more completely to engage in co-ordinated interaction that harms consumers. Co-ordinated interaction is comprised of actions by a group of firms that are profitable for each of them only as a result of the accommodating reactions of the others. This behaviour includes tacit or express collusion, and may or may not be lawful in and of itself.

30. Successful co-ordinated interaction entails reaching terms of co-ordination that are profitable to the firms involved and an ability to detect and punish deviations that would undermine the co-ordinated interaction. Detection and punishment of deviations ensure that co-ordinating firms will find it more profitable to adhere to the terms of co-ordination than to pursue short-term profits from deviating, given the costs of reprisal. In this phase of the analysis, the agencies will examine the extent to which post-merger market conditions are conducive to reaching terms of co-ordination, detecting deviations from those terms, and punishing such deviations. Depending upon the circumstances, the following market factors, among others, may be relevant: the availability of key information concerning market conditions, transactions and individual competitors; the extent of firm and product heterogeneity; pricing or marketing practices typically employed by firms in the market; the characteristics of buyers and sellers; and the characteristics of typical transactions.

31. Certain market conditions that are conducive to reaching terms of co-ordination also may be conducive to detecting or punishing deviations from those terms. For example, the extent of information

b) Firms Distinguished Primarily by Their Capacities. Where products are relatively

42. A merger having anticompetitive effects can attract committed entry, profitable at premerger prices, that would not have occurred premerger at these same prices. But following the merger, the reduction in industry output and increase in prices associated with the competitive effect of concern may allow the same entry to occur without driving market prices below premerger levels. After a merger that results in decreased output and increased prices, the likely sales opportunities available to entrants at premerger prices will be larger than they were premerger, larger by the output reduction caused by the merger. If entry could be profitable at premerger prices without exceeding the likely sales opportunities -- opportunities that include pre-existing pertinent factors as well as the merger-induced output reduction -- then such entry is likely in response to the merger.

43. The third step assesses whether timely and likely entry would be sufficient to return market prices to their premerger levels. This end may be accomplished either through multiple entry or individual entry at a sufficient scale. Entry may not be sufficient, even though timely and likely, where the constraints on availability of essential assets, due to incumbent control, make it impossible for entry profitably to achieve the necessary level of sales. Also, the character and scope of entrants' products might not be fully responsive to the localised sales opportunities created by the removal of direct competition among sellers of differentiated products. In assessing whether entry will be timely, likely, and sufficient, the agencies recognise that precise and detailed information may be difficult or impossible to obtain. In such instances, the agencies will rely on all available evidence bearing on whether entry will satisfy the conditions of timeliness, likelihood, and sufficiency.

7.4 Efficiencies Anaheroiu8.5(ac)11(t)18..41310.5(udif)8.850.4iiavaFouheance0ers a.(a)-3. 9(a)-3.3(ny.0856 e

making this determination; the agencies will not insist upon a less restrictive alternative that is merely theoretical.
48. Efficiencies are difficult to verify and quantify, in part because much of the information relating to efficiencies is uniquely in the possession of the merging firms. Moreover, efficiencies projected reasonably and in good faith by the merging firms may not be realised. Therefore, the merging firms must substantiate efficiency claims so that the agencies can verify by reasonable means the likelihood and magnitude of each asserted efficiency, how and when each would be achieved (and any costs of doing so), how each would enhance the merged firm's ability and incentive to compete, and why each would be merger-specific. Efficiency claims will not be considered if they are vague or speculative or otherwise cannot be verified by reasonable means.

49. *Cognisable efficiencies* are merger-specific efficiencies that have been verified and do not arise from anticompetitive reductions in output or service. Cognisable efficiencies are assessed net of costs produced by the merger or incurred in achieving those efficiencies.

50. The agencies will not challenge a merger if cognisable efficiencies are of a character and magnitude such that the merger is not likely to be anticompetitive in any relevant market. To make the requisite determination, the agencies consider whether cognisable efficiencies likely would be sufficient to reverse the merger's potential to harm consumers in the relevant market, *e.g.*, by preventing price increases in that market. In conducting this analysis, the agencies will not simply compare the magnitude of the cognisable efficiencies with the magnitude of the likue.1(itude)-18.4(th t)8.4(h)2(i)-2.toteni-18.4e8t2.6(c318.8sayev19.

54. A merger is not likely to create or enhance market power or facilitate its exercise if the following circumstances are met:

a) the allegedly failing firm would be unable to meet its financial obligations in the near future;

b) it would not be able to reorganise successfully under Chapter 11 of the Bankruptcy Act;

c) it has made unsuccessful good-faith efforts to elicit reasonable alternative offers of acquisition of the assets of the failing firm that would both keep its tangible and intangible assets in the relevant market and pose a less severe danger to competition than does the proposed merger; and

d) absent the acquisition, the assets of the failing firm would exit the relevant market.

8. Other Public Interest Considerations in Merger Review

55. The United States antitrust agencies do not employ a "public interest" test in analysing mergers. "The unifying theme of the Guidelines is that mergers should not be permitted to create or enhance market power or to facilitate its exercise . . .. While challenging competitively harmful mergers, the Agenc[ies] seek[] to avoid unnecessary interference with the larger universe of mergers that are either competitively beneficial or neutral." GUIDELINES 0.1

56. For many years, a United States regulatory agency for the airline industry applied a public interest test in the specific case of mergers in the airline industry. After forty years of experience with that test, it was generally not viewed as useful or necessary, and the separate test was eliminated when the

from two to one, and that a reduction from three competitors to two was not of concern. Following implementation of the merger, there was a massive service breakdown in the West, resulting in billions of