RECENT DEVELOPMENTS IN MERGER ENFORCEMENT

Address by

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Before the

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THE SHERATON TUCSON EL CONQUISTADOR
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It is a pleasure to be here with you today, and in such a nice setting. Before taking questions, I thought I would talk for a minute about the Department’s current approach to merger enforcement, which does not diverge significantly from past Administrations, and about some recent developments about which you should be aware.

**Approach to Merger Analysis**

Those of you who do antitrust work know that our approach to horizontal merger analysis is described generally in the 1992 Horizontal Merger Guidelines, issued jointly by the Department and the Federal Trade Commission. As these Guidelines make clear, our review focuses on whether the merger would create or enhance market power, or facilitate its exercise. Market power, from a seller's point of view, is the power profitably to maintain prices above competitive levels, or to reduce output, product quality, service, or innovation.

Our approach to horizontal merger analysis is first to define economically meaningful markets, along relevant product and geographic lines, assign market shares, and assess whether the merger would increase concentration significantly -- to the point that post-merger concentration levels would be high.
We then assess whether anticompetitive effects are likely, given these concentration levels and other characteristics of the market. As the Horizontal Guidelines explain, we look to two possible sources of anticompetitive effects. We look to whether the merger would permit the newly combined entity unilaterally to raise prices. We also look to whether the merger would encourage or facilitate explicit or tacit collusion -- where multiple sellers coordinate their activities, to the point, perhaps, of simulating collectively the behavior of a single firm monopolist.

Finally, we assess whether new entry and/or product repositioning would constrain price increases; whether there are efficiency gains associated with the merger that outweigh any anticompetitive effects; and whether, but for the merger, either party to the transaction would be likely to fail, causing its assets to exit the market.

Our approach to vertical mergers is ably summarized in a speech delivered last year by my predecessor, Steve Sunshine. Our analysis of vertical mergers is far more complex, although it focusses, as before, on whether the transaction gives the merged firm the ability and the incentive to raise prices or reduce output to customers in

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1 See "Vertical Merger Enforcement Policy," Remarks by Steven C. Sunshine, Deputy Assistant Attorney General, Antitrust Division, U.S. Department of Justice, before the ABA Section of Antitrust Law Spring Meeting, April 5, 1995.
the downstream market. Typically, for this to happen, the upstream and downstream markets must both be conducive to the exercise of market power, as determined pursuant to the 1992 Horizontal Merger Guidelines analysis. Where this is the case, a vertical merger may have anticompetitive effects by raising the costs of a non-integrated rival, foreclosing rivals’ access to vital inputs or customers, raising barriers to entry, facilitating coordinated interaction, or avoiding regulatory requirements. Again, efficiencies are an important consideration as well.

There are three important points to emphasize about our application of these principles:

1. The Division only challenges mergers that hurt consumers -- that is, hurts consumers by raising prices, or by reducing product output quality, service or innovation. This is true whether the merger involves parties that are horizontal competitors, or parties with a vertical relationship. Our reviews of mergers are not driven by concerns about the market positions of particular competitors, or protecting existing supply relationships.

2. We recognize that the vast majority of mergers are competitively neutral or even beneficial for
competition and consumers. This may be because they create synergies, improve or create new products, and/or lower costs. We recognize that vertical mergers, in particular, often create efficiencies. Only a very small percentage of mergers are challenged each year by the Division.

3. For both of these reasons, we do not approach merger analysis mechanistically. The Horizontal Guidelines themselves provide that we will apply them reasonably and flexibly, taking into account all of the facts and circumstances surrounding the merger. Likewise, our approach to vertical mergers is cautious and case specific.

In particular, market definition, the assignment of market shares, and the assessment of concentration in the market are only starting points in our analysis. We consider alternative market definitions in our analysis, and we take seriously our charge to consider reasons why market shares might overstate or understate a firm's competitive strength in the market. We take foreign competition into account and study entry conditions and possible efficiencies.

I would urge any of you with mergers before our agency to come in and tell us your story. If you believe your merger is good for consumers, tell us why. I can assure you
we will listen. Our policy is to be open and candid about what we believe the issues may be and to work with you and your outside counsel and economists to resolve them.

**Current Merger Wave**

Among the more important developments in the merger area, as far as I am concerned, is the size and strength of the current merger wave, which is presenting quite a challenge to our merger enforcement program.

Last year's merger activity was literally unprecedented, both in terms of volume and value. By one count, 8,956 mergers were announced last year, worth a total of $457.88 billion. This is well over $1 billion a day. Merger activity cut across a variety of sectors, from banking to electric power, information technology, computer software, media, health care and others.

As you would expect, this increase in merger activity has translated into an increased workload at the Division:

- The number of transactions reported to us under Hart-Scott-Rodino jumped from 2,301 in fiscal year 1994 to 2,815 in 1995 -- an increase of over 500 transactions.
- The number of merger investigations increased from 105 in fiscal year 1994 to 133 in 1995, the highest number of merger investigations in a decade.
• Second requests increased from 30 to 37.

• This rapid pace of HSR filings, investigations, and second requests have continued in the first few months of fiscal 1996.

And we are proud of the results we have achieved. We have enforced the law aggressively where necessary, but that has been in only a small minority of transactions we have reviewed. And most of our challenges result in settlements that permit the bulk of the transactions to go forward:

• We filed formal challenges to a total of nine mergers in court in 1995, settling six of these with consent orders that allowed the bulk of each transaction to go forward.

• Seven additional transactions were restructured in 1995 as a result of the Division's investigation, without the filing of a formal complaint.

• The pace of successful challenges has also continued in the early months of fiscal year 1996. Since October 1, we have filed three formal challenges, settling all three, and four mergers were restructured by the parties without a formal challenge. I'm going to talk about two of these recent cases in a minute.

With all of this activity in the merger area, we are bracing for even more as a result of the enactment of the new telecom legislation. We believe that new legislation will increase merger activity in the telecom area for two
reasons. First, the bill provides opportunities for telecommunications firms to enter new markets. In many cases such entry will occur via acquisition.

Second, the bill relaxes certain media ownership limitations. The bill eliminates or relaxes, for example, the current FCC limit on the number of TV and radio stations that a single person or entity may hold nationwide, restrictions on multiple ownership in local markets, and various media cross-ownership restrictions, such as rules prohibiting a single entity from owning both TV and radio stations in a given local market, both a TV station and a cable system, or both a TV broadcast network and a cable system. In addition, the FCC is undertaking a review of all of their existing multiple ownership rules which may well lead to the lessening or repeal of other restrictions, such as the ban on owning more than one television stations in a local market. We can expect to see potentially significant merger activity involving telephone companies among radio and TV broadcasters and among the other media players that I mentioned.

Recent Cases

I think two of our more recent, more visible cases illustrate our surgical approach to merger enforcement, and three other trends in merger enforcement at the Division that I would like to highlight. The first transaction is Kimberly-Clark's $6.8 billion acquisition of Scott Paper
Kimberly-Clark and Scott Paper sell a wide variety of paper and other consumer products, of course. In the course of our investigation, however, we developed a concern about only two products, facial tissue (a $1.3 billion market) and baby wipes (a $500 million market). After the merger, the combined entity would have had over a 50 percent market share in each of these two markets. There were few other sizable competitors, little imports, no asserted efficiencies, and entry into these markets was difficult.

To resolve our competitive concerns in the two markets we identified, the parties agreed to divest the Scotties brand name, a significant amount of tissue manufacturing capacity, Scott's baby wipes plant in Delaware, and associated brand names and other tangible and intangible assets. The rest of the transaction was permitted to proceed. Together with the State of Texas, we filed a formal complaint challenging the acquisition in U.S. district court in Dallas, along with a proposed consent order embodying our settlement with the parties. ²

The Disney/ABC transaction was a little more complex. Disney had significant interests in the production,
syndication and distribution of TV programming, both through broadcast stations and cable networks, including its own premium cable service, The Disney Channel. It also owned a VHF broadcast station in Los Angeles, KCAL-TV. Likewise, Capital Cities/ABC had significant interests in both TV production and distribution, most prominently through the ABC national television network, numerous national cable networks, and owned and operated groups of TV broadcast stations, including one in Los Angeles.

This transaction presented both horizontal and vertical issues. First, we sought to ensure that the combination of Disney and ABC did not increase concentration unacceptably and have anticompetitive effects horizontally at any of the various levels of TV production and distribution impacted by the merger. Second, we needed to ensure that the vertical combination of Disney's significant presence in TV program production and ABC's strong presence in programming distribution would not result in competitive foreclosure, i.e., that ABC's competitors in the market for distribution would not be foreclosed from access to vital TV programming, and that Disney's competitors in the market for programming supply would not be foreclosed from access to distribution outlets.

After a lengthy investigation, we disposed of the vertical issues to our satisfaction. As I mentioned, we take a focused, fact-based approach to vertical merger
analysis. In the course of our investigation, we were also able to eliminate all but one of the horizontal issues. We were in the midst of analyzing the impact of combining the two TV broadcast stations under common ownership in Los Angeles when Disney decided voluntarily to divest one of the two stations, effectively mooting that part of investigation. We negotiated with Disney an agreement designed to ensure that it would follow through with its divestiture plans, pursuant to applicable FCC regulatory processes.3

Trends In Merger Analysis

These two cases illustrate three recent trends in merger enforcement at the Division. First, as illustrated in the Kimberly-Clark/Scott Paper matter, we at the Division are working more and more closely with the state attorneys general. In this case, and increasingly in such cases generally, we are working hand-in-hand with interested states from the beginning of our investigations, interviewing and even deposing witnesses together, sharing documents where the parties consent or where the law otherwise permits, and even negotiating consent decrees and filing formal complaints together.

3 See Letter from Anne K. Bingaman, Assistant Attorney General for the Antitrust Division, U.S. Department of Justice, to the Honorable Reed E. Hundt, Chairman, Federal Communications Commission (January 16, 1996).
Increased cooperation with the states has been one of the top priorities of the head of our Division, Assistant Attorney General Anne Bingaman. This is true across areas of antitrust enforcement, including criminal and civil nonmerger enforcement coordination. In the merger area, coordination with the states has been most common in bank mergers, but as I say, it is spreading throughout our merger program.

Federal-state cooperation certainly makes sense from a resource point of view. In an era of tight budgets, the public expects all of us in law enforcement to combine resources and to operate as efficiently as possible. It also make sense from a philosophical standpoint. The more we interact, the more consistent antitrust enforcement will be across the board.

Both rationales for federal-state cooperation were evident in the Kimberly-Clark case. The Texas Attorney General coordinated the activities of all of the interested states. I am quite confident that the costs of the investigation were reduced, both for the parties to the merger and for the government parties. And as I mentioned, the Department and the State of Texas joined in filing the same complaint and negotiating the same, internally consistent settlement.

The second trend illustrated by the Kimberly-Clark case is the continuing refinement of the Division's approach to
mergers that threaten unilateral anticompetitive effects. As I mentioned, a merger may be anticompetitive even if it does not increase the risks of explicit or tacit collusion, if it enables the merged firm unilaterally to raise the price of one or more of the products of the merging companies. This may be possible, for example, in differentiated product markets to the extent that some of the lost sales due to the price increase are merely diverted to the product of the merger partner. Depending on the extent of such diversion and the relative price-cost margins, this price increase may be profitable after the merger when it was not profitable before.

The theory of unilateral effects is not new. What is new is the continuing refinement of the Division's approach to predicting and measuring such effects using sophisticated, econometric techniques. 4

Where consumer products are involved, such as facial tissue and baby wipes, that are scanned at retail checkout counters, we often have access to detailed price and quantity data over time. Our economists can then model the demand for such products, estimate demand elasticities, and predict the price increases that would flow from post-merger profit maximizing behavior. Such techniques were employed

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4 For an excellent summary of the Division’s current approach, see Shapiro, "Mergers With Differentiated Products," Antitrust (Spring 1996), page 23.
to predict significant price increases for facial tissue and baby wipes following the Kimberly-Clark/Scott merger, and contributed greatly to our investigation, along with more traditional analytic techniques.

The final trend that I think is illustrated by these recent cases is an increasing degree of flexibility in negotiating remedies when mergers are found to be anticompetitive. There is every reason to be somewhat flexible. We want to take concrete, enforceable steps to ensure that competition is not lost as a result of the merger; but we want also to avoid unnecessary harm to the merged company, and to minimize the loss of any efficiencies associated with the merger. We also want to make sure that the purchaser of any divested assets has the assets it needs to be an effective competitor in the market.

The traditional remedy for horizontal merger problems has been divestiture of specified assets pursuant to a consent order. In Kimberly-Clark, however, we took the unusual approach of identifying four tissue plants that would be potentially subject to divestiture, but at the same time providing that a buyer could select one or at most two of these plants from this menu of choices. We felt that this would both reduce the size of the ultimate divestiture package, and ensure that the buyer's needs could be accommodated to the greatest possible extent. And in Disney, we took the unusual step of agreeing to a consent
order requiring divestiture, but agreeing not to file it with the court right away, in light of Disney's voluntary commitment to sell KCAL-TV in Los Angeles, and the expectation that the FCC would enter an enforceable order requiring the sale. Other examples of flexibility at the remedy stage abound, but I will stop there in the interest of time and take any questions you may have.

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5 See, e.g., United States v. Morton Plant Health System, Inc., C. No. 94-748-CIV-T-23E (M.D. Fla, filed May 5, 1994) (Settlement bars merger of two hospitals, while permitting them to act jointly in providing certain health care services).