EDITOR'S NOTE

Conduct Merger Remedies: Tried But Not Tested

BY DEBORAH L. FEINSTEIN

THE DEPARTMENT OF JUSTICE HAS recently resolved a number of mergers the Department viewed as antitcompetitive with remedies that have been variously characterized by observers as conduct remedies, regulatory remedies, a departure from past practice, and downright unusual.[1] A brief review of remedy pronouncements over the years, however, makes clear that while divestitures are now and have been the favored remedy, the U.S. authorities (as well as their counterparts in other jurisdictions) have regularly accepted remedies other than divestitures when they believed such alternatives were warranted, particularly in vertical transactions. Given the resurgence in vertical cases—and accompanying conduct remedies—it is time to evaluate the effectiveness of such remedies.

Evolution of Remedies in Merger Transactions

In the past, merger remedies were limited by practicalities. For decades, the agencies investigated most transactions after they were consummated. The inevitable scrambling of the eggs made obtaining effective remedies difficult. After the Hart-Scott-Rodino Act was implemented it became easier to craft effective remedies. Required divestitures became routine, and parties often went in at the outset of a transaction to offer divestitures to fix troubling aspects of the transaction, while pressing for approval of the rest of the transaction.

Along the way, remedies became more creative. During the late 1980s and early 1990s, the FTC and DOJ accepted a number of remedies that required licensing instead of a divestiture. For instance, in *Hollis/Electrovert*, the DOJ required that Electrovert grant North American rights to all of Hollis's wave soldering technology to any two other firms presently selling wave soldering machines in the United States.[2] In *Rhone-Poulenc S.A.*, the FTC required Rhone-Poulenc to license the dairy cultures of Marschall's, the entity it acquired, for $50 to all comers (with the exception of certain key competitors).[3] Yet, even while accepting these remedies, the agencies were quick to make clear that licensing was "a remedy that is generally less favored . . . . In addition, the Commission has neither the resources nor the inclination to . . . [police] the . . . technical and legal controversies inherent in such provisions."[4]

Approximately twenty years after the HSR Act was implemented, the FTC Bureau of Competition studied the effectiveness of the remedies it obtained in merger proceedings.[5] The FTC Divestiture Study found that while divestitures had largely been successful, features of the divestiture orders, as well as the dynamics of the divestiture process, affected the extent of the success of those remedies. The study focused only on divestitures. Thus, while indicating that the Bureau was "experimenting with a new type of remedy . . . the so-called 'licensing remedy,'" the study did not address its effectiveness.

The FTC Divestiture Study articulated key findings that remain the principles that underlie the Bureau's preferred merger remedies today—that divestitures of ongoing businesses succeeded at a higher rate than divestitures of selected assets and that continuing relationships, such as supply agreements, between the merged company and the buyer of divested assets post-divestiture may increase the vulnerability of buyers of divested assets but may be critical to the success of some buyers. These principles are reflected in the Bureau's Guide to Negotiating Remedies.[6]

Yet, while the agencies expressed a preference for divestitures and strengthening the specifics of divestiture orders, the mid-90s also saw mergers (mostly vertical in nature) remedied with conduct provisions. One notable case was *Primestar*. In that case, the DOJ had concerns that a joint venture of cable companies could restrict access to programming. The remedy was a consent decree precluding the joint venture from obtaining exclusive content unless a rival obtained reasonably comparable content on an exclusive basis.[7] Another example is Time Warner's acquisition of Turner Broadcasting. In that case, one of the FTC's concerns was that Time Warner could raise prices of the Turner programming to third parties and undermine the incentives of TCI, a cable operator, to distribute competitive programming because of its ownership interest in Time Warner. The consent included provisions that (1) required TCI, Turner and Time Warner to cancel their long-term carriage agreements; (2) barred Time Warner's programming interests from discriminating in price against rival cable systems; (3) prohibited Time Warner's cable interests from discriminating in carriage decisions against rival programmers; and (4) required Time Warner's cable interests to carry a rival to CNN.[8]

That same time period also saw a spate of defense mergers. Those cases generally raised concerns that the merged firm would favor itself as a subcontractor or, through vertical integration, have access to information of its rivals that could lessen competition. Typically, remedies in those matters were firewalls to prevent the inappropriate sharing of

Deborah L. Feinstein, Editorial Board Chair of ANTITRUST, *is a Partner at Arnold & Porter LLP, where her practice focuses on representing merging parties before the FTC and DOJ. She represented GE in its sale of a majority interest in NBCU to Comcast.*

competitively sensitive information.[9] Similarly, the *Merck/Medco*[10] and *Lilly/PCS*[11] decrees resolved the issues arising from the combination of pharmaceutical companies and downstream pharmacy benefit managers through conduct provisions, such as firewalls.

In June, the Antitrust Division issued a new Policy Guide to Merger Remedies.[12] The Guide continues to focus on structural relief, typically divestitures, as the solution to horizontal mergers. It also discusses conduct remedies, although primarily in the context of vertical mergers. Rather than suggesting conduct remedies are disfavored, the new Guide now indicates that "[c]onduct remedies can be an effective method for dealing with competition concerns raised by vertical mergers and also are sometimes used to address concerns raised by horizontal mergers (usually in conjunction with a structural remedy)."[13]

Current Thinking on Remedies

In light of the latest consent decrees, remedy guide and divestiture reports, what is the state of U.S. remedy policy?

Divestitures continue to be the remedy of choice—and with extremely rare exceptions, the only remedy for horizontal mergers at both the FTC and DOJ. In fiscal years 2010 and 2011, 18 of 19 horizontal merger decrees required divestitures. Some read the focus on conduct remedies as a significant departure from past practice. However, the recent increase in remedies other than divestitures can be interpreted not so much as a shift in policy as, in large measure, a result of the vertical nature of the matters. *Comcast/NBCU*, *LiveNation/Ticketmaster*, *Google/ITA*, and the acquisitions by PepsiCo and Coca-Cola of their downstream bottlers were all, in whole or in part, vertical transactions in which the efficiencies of the transaction would have been lost were divestitures required. Indeed, in a recent speech at the Antitrust Enforcement Symposium, the Antitrust Division's General Counsel noted that there were more vertical cases last year than in any year since 1994.

There is remarkable convergence of the key enforcement agencies outside the United States as to the preference for divestiture remedies. This should allow companies to resolve issues in many cases with a consistent divestiture across multiple jurisdictions. Going back to 2004 in *GE/Instrumentarium*,[14] the agencies have worked to make sure their divestiture requirements are not in conflict. The Final Judgment in that case was the first to reference that the EC would also be involved in enforcing the divestiture requirement. The DOJ's Final Judgment, *inter alia*, defined the assets to be divested with reference to the parties' commitments to the EU (¶ II.E.) and provided that any trustee would be chosen in conjunction with the EC (¶¶ III.A and C).[15]

Nevertheless, despite broad consensus, there will be differences in approach. In cases—both recent and older—the EU has required remedies in cases involving interoperability between devices offered by different companies where the U.S. agencies have declined to do so. For instance, in the *Intel/McAfee* matter, the EC required Intel to disclose information and provide technical assistance so that competing security software vendors could take advantage of new Intel microprocessor features.[16] On the same facts, the FTC required no relief.

As transactions and theories become more complex, so too will the remedies. A theory involving the foreclosure of a potential competitor in a rapidly evolving industry will hardly require the same remedy as the horizontal merger of supermarkets. And sometimes remedies are affected by the fact that multiple agencies have jurisdiction over the matter. Certainly, in the Comcast transaction, the DOJ was likely influenced by its discussions with the FCC over the approach to the transaction. In other cases, the need for global competitive authorities to avoid having conflicting remedies may lead to compromise. Finally, of course, there are simply times when messy facts make for messy remedies, which may be the only good explanation for why the DOJ resolved a consummated horizontal merger with a requirement that the acquiror promise to make repairs to its facilities.[17]

Analyzing the Effectiveness of Merger Remedies

Over the years, the consideration of what makes an effective remedy has continued. In 2005, the EC conducted a Merger Remedies Study.[18] Like the FTC Divestiture Study, the EC's report found that most divestitures were effective, but certain features, such as divestitures of ongoing businesses, hold separates, and monitors, could enhance the effectiveness of the divestiture. The EC followed with a Remedies Notice, which, among other things, emphasized a preference for structural relief in the form of divestitures but indicated that conduct remedies could be appropriate in certain cases.[19]

Most recently, Canada conducted a study on remedies through a series of interviews. Like the FTC did in its Divestiture Study, the Canadian Competition Bureau found that while the required divestitures were largely completed, the divestiture packages were not always of good quality, assets were not always maintained pending divestiture, and the quality of the purchaser made a difference in the likelihood of the effectiveness of the divestiture.[20]

It has been over fifteen years since the FTC Divestiture Study, and the Justice Department has not in recent times conducted such a study. Is it now time for a merger retrospective focused on conduct remedies? In general, more study is always useful. A study might show that conduct remedies are perfectly appropriate and silence the critics who find these remedies too novel. Or it may suggest tweaks to conduct remedies that can improve them, much as the FTC's Divestiture Study did for divestitures. And it is always possible that a study will show that such remedies have been insufficient in preserving the competitiveness of a market.

There are, of course, considerable challenges in conducting any retrospective study of merger remedies, particularly those involving nonstructural relief. Unlike the case of divestitures where a primary question is simply, "Did the divestiture occur?," the question of "Did the remedy take place?" may be more difficult to answer. For instance, where firewalls are to be erected, or companies are required to treat products on a nondiscriminatory basis, it may not be an easy yes or no answer as to whether the remedial requirements were observed. An ongoing monitor—often required with conduct consents—may assist in determining, e.g., that an appropriate firewall was erected.

Answering the question of whether competition has been maintained is very challenging. Determining how much competition would have existed between the parties but for the merger is a difficult predictive task, which the agencies do only in broad strokes during the course of a merger investigation. They simply need to determine that there is competition that would be eliminated. Assessing how much competition, what would have happened to prices, and which specific innovations may have come about is not typically part of the exercise. Further complicating the effort is that in a post-remedy retrospective, the agencies rarely have access to the necessary documents and data to answer these questions.

These assessments are made more difficult when the agency's concern is not about preserving existing competition, but future potential competition. For instance, in the *Comcast/NBCU* matter, one significant concern was the elimination of potential online competitors by foreclosing such future competitors from important NBCU content. The complaint makes clear that such competition was "nascent" and that online competitors have "begun" to provide competition.[21] The DOJ consent decree provided the terms on which such potential entrants could have access to NBCU content and to enter arbitration if the parties could not come to terms on an agreement for the content. But what if no third party requests the content? Does that mean the consent failed—or simply that the possibility of future competitors simply did not arise?

Any assessment of the effectiveness of the remedies—and the impact on competition—must of course be considered in conjunction with the efficiencies arising from the transaction, a particularly important aspect of vertical transactions. In many of the vertical transactions the agencies have analyzed, the elimination of double marginalization was a significant procompetitive benefit that could arise from the transaction. If such a benefit arose, the result might be that the merging parties would increase their market share—making it appear that other competitors were less able to compete. In reality, however, the increase might actually be the result of the merged firm lowering its costs (and thus its prices) and becoming more profitable.

Past retrospectives have faced these same challenges—particularly the difficulty of getting the type of data one might like to use to assess what has happened to prices, market shares, and the like. Instead, they have simply asked various parties their views—as was done in the FTC Divestiture Study, the EC Remedies Study, and the Canadian Merger Remedies Study. While far from perfect, a backwards look at some of these remedies—when sufficient time has passed—would further the agencies' laudable efforts to "use a scalpel instead of a sledgehammer" in remedying transactions. ■

1 *See, e.g,*, Helen Thomas, *Antitrust Chief Stressed Negotiation at DOJ*, Fin. Times, Sept. 6, 2011, at 18 (describing the "flurry of so-called conduct remedies" as reflective of former DOJ Antitrust Division head Christine Varney's pragmatic approach to merger enforcement).

2 Press Release, Antitrust Suit and Proposed Consent Decree Filed in Hollis Automation/Electrovert U.S.A. Acquisition (Sept. 29, 1992), *available at* http://www.justice.gov/atr/public/press_releases/1992/211300.htm.

3 Rhone-Poulenc S.A., 113 F.T.C. 329, 1990 WL 10012625, at *4 (1990).

4 Mary Lou Steptoe & Deborah L. Feinstein, *Merger Remedies*, Int'l Merger L., Mar. 1991, at 14.

5 Fed. Trade Comm'n, Bureau of Competition, A Study of the Commission's Divestiture Process (1999) (FTC Divestiture Study), *available at* http://www.ftc.gov/os/1999/08/divestiture.pdf.

6 Fed. Trade Comm'n, Bureau of Competition, Negotiating Merger Remedies (2003), *available at* http://www.ftc.gov/bc/bestpractices/bestpractices030401.pdf.

7 United States v. Primestar Partners, L.P., Civ. A. No. 93 Civ. 3913 (JES), 1994 WL 196800, at *3 (S.D.N.Y. Apr. 4, 1994).

8 Press Release, Fed. Trade Comm'n, FTC Requires Restructuring of Time Warner/Turner Deal: Settlement Resolves Charges that Deal Would Reduce Cable Industry Competition (Sept. 12, 1996), *available at* http://www.ftc.gov/opa/1996/09/timewarn.shtm.

9 *See, e.g.*, United States v. Raytheon Co., No. 1:97CV02397, 1997 WL 669646 (D.D.C. Oct. 22, 1997); Boeing Co., 61 Fed. Reg. 66,038 (FTC Dec. 16, 1996); Raytheon Co., 61 Fed. Reg. 31,526 (FTC June 20, 1996); Lockheed Martin Corp., 61 Fed. Reg. 18,732 (FTC Apr. 29, 1996); Silicon Graphics, Inc., 60 Fed. Reg. 35,032, 1995 WL 390510 (FTC July 5, 1995); Lockheed Corp., 60 Fed Reg. 5408 (FTC Jan. 27, 1995).

10 Merck & Co., 63 Fed. Reg. 46,451–01 (FTC Sept. 1, 1998).

11 Eli Lilly and Co., 59 Fed. Reg. 60,815–01 (FTC Nov. 28, 1994).

12 U.S. Dep't of Justice, Antitrust Division Policy Guide to Merger Remedies (June 2011), *available at* http://www.justice.gov/atr/public/guidelines/272350.pdf.

13 *Id.* at 12.

14 United States v. General Elec. Co., No. Civ. A. 03-1923, 2004 WL 602773 (D.D.C. Feb. 23, 2004).

15 *Id.* at *4.

16 Case No. COMP/M.5984—Intel/McAfee, Comm'n Decision at 63 (Jan. 26. 2011), *available at* http://ec.europa.eu/competition/mergers/cases/decisions/m5984_20110126_20212_1685278_EN.pdf.

17 Proposed Final Judgment at 3, United States v. George's Food LLC, Civ. A. No. 5:11-cv-00043 (June 23, 2011), *available at* http://www.justice.gov/atr/cases/f272400/272495.pdf.

18 European Comm'n, Directorate Gen. of Competition, Merger Remedies Study (Oct. 2005), *available at* http://ec.europa.eu/competition/mergers/legislation/remedies_study.pdf.

19 Commission Notice on Remedies Acceptable Under Council Regulation (EC) No. 139/2004 and Under Commission Regulation (EC) No. 802/2004, 2008 O.J. (C 267) 1.

20 Competition Bureau Canada, Competition Bureau Merger Remedies Study 4–6 (2011), *available at* http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/vwapj/cb-merger-remedy-study-summary-e.pdf/$FILE/cb-merger-remedy-study-summary-e.pdf.

21 Complaint at 3, 21, United States v. Comcast Corp., No. 1-11-CV-00106 (D.D.C. Jan.18, 2011), *available at* http://www.justice.gov/atr/cases/f266100/266164.pdf.