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Comments of the Competitive Enterprise Institute

RE: FTC-DOJ Merger Guidelines

Matter No.: P859910

The authors of this submission first want to thank the Federal Trade Commission (FTC) and the Department of Justice (DOJ) for the opportunity to respectfully comment on the 2023 Draft Merger Guidelines released on July 19, 2023. We are employees of the Competitive Enterprise Institute, a non-profit research and advocacy organization that focuses on regulatory policy.

The Draft Merger Guidelines purport to "explain how the Department of Justice and the Federal Trade Commission (the 'Agencies') identify potentially illegal mergers," and "help the public, business community, practitioners, and courts understand the factors and frameworks the Agencies consider when investigating mergers."[1] Unfortunately, the content of the Draft Guidelines rely on bad economics and a distorted picture of how antitrust law is currently applied in the courts. To avoid the harms this flawed guidance will inflict, the Agencies should reconsider them in the ways that follow. The discussion below is in no way an exhaustive account of the problems contained in the Draft Guidelines.

New guidelines do not sufficiently account for the possible benefits of a merger.

In the Draft Merger Guidelines, the Agencies put their thumbs on the scale of justice with a presumption that mergers are de facto harmful to competition. This presumption will ultimately lead to an increase of Type I errors.[2] Too many procompetitive and efficient mergers will face undue scrutiny. As the current FTC's record in challenges to mergers in Article III courts already shows, mergers that are not, in fact, anticompetitive will be unsuccessfully challenged under that

[1] U.S. Department of Justice and Federal Trade Commission, Draft Merger Guidelines, July 19, 2023, p. 1, https://www.ftc.gov/system/files/ftc_gov/pdf/p859910draftmergerguidelines2023.pdf.

[2] Type I errors are false-positives, while type II errors are false-negatives. Some argue that "the cost of making a Type I error are higher (stopping or slowing procompetitive innovation), but the cost of making a Type II error is lower (because these errors can often be mitigated by natural market forces or standard antitrust law) in competitive markets." Babette Boliek, "Type I Vs Type II Errors: Antitrust Lessons for Communications Policy," AEIdeas (blog), American Enterprise Institute, February 5, 2014, https://www.aei.org/technology-and-innovation/telecommunications/type-vs-type-ii-errors-antitrust-lessons-communications-policy/.

presumption.[3] This is a waste of taxpayer money and resources that the agencies could be employing instead with productive actions.

Even at current merger enforcement levels, Columbia Law School's blog on Corporations and the Capital Markets reports that the process is costly with "filing charges, legal expenses, and, when the deal fails, breakup fees." Included are the indirect and harder to quantify costs of "delay and uncertainty of a lengthy review process during which deal financing must be kept in place and anxious employees and customers reassured." The authors also note that the process incentivizes offsetting of those costs by hiring lobbyists, finding that the "annual acquirer lobbying expenditure amounts on average to $3 million."[4] Increased merger challenging activity will in turn increase these costs for American businesses.

Generally, the Draft Guidelines fail to consider the benefits of mergers and acquisitions. Guideline 9 provides a helpful example. It states, "If an individual transaction is part of a firm's pattern or strategy of multiple acquisitions, the Agencies consider the cumulative effect of the pattern or strategy."[5] It goes on to reference the populist political debate of the time, but does not mention the economic and consumer welfare focused reforms to antitrust law in the past four decades.

To ignore the possible benefits of a merger, as these guidelines do, is to miss the bigger, more comprehensive picture in the U.S. economy. Specifically, while there may be a certain percentage of "killer acquisitions" in the US economy,[6] there are also strong incentives for acquiring firms to improve the product or service of the acquired firm. These benefits must be taken into consideration and not dismissed out of hand when initially weighing anticompetitive concerns in merger approval.

A good example is Facebook's (now Meta's) purchase of the then-fledgling mobile application Instagram. Facebook's superior resources and expertise took Instagram from a glitchy app to one with a billion users.[7] Since the purchase, Meta has consistently worked to improve the Instagram-user experience and attended to technical-compatibility issues. Meta has also been

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[3] Merger challenges lost by current FTC include Meta/Within, Microsoft/Activision, Booze Allen Hamilton/EverWatch, UnitedHealth/Change Healthcare, US Sugar/Imperial Sugar

[4] Jana P. Fidrmuc, Peter Rosenboom, and Eden Quxian Zhang, "The Costs of M&A Antitrust Review and Acquirer Lobbying," The CLS Blue Sky Blog (blog), Columbia Law School, January 10, 2018, https://clsbluesky.law.columbia.edu/2018/01/10/the-costs-of-ma-antitrust-review-and-acquirer-lobbying/.

[5] Draft Merger Guidelines, p. 4.

[6] A killer acquisition is often defined as "when a company acquires control of an innovative company to eliminate them as a possible source of future competition." Marc Mossé and David Bosco, "A 'Killer Acquisition' Is When a Company Acquires Control of an Innovative Company to Eliminate Them as a Possible Source of Future Competition," August Debouzy (blog), January 16, 2023, https://www.august-debouzy.com/en/blog/1891-a-killer-acquisition-is-when-a-company-acquires-control-of-an-innovative-company-to-eliminate-them-as-a-possible-source-of-future-competition.

[7] Jessica Melugin, "Facebook Acquisitions Benefitted Its Employees, Sellers, and Consumers. Where Is the Harm?," *National Review*, December 10, 2020, https://www.nationalreview.com/2020/12/facebook-acquisitions-benefitted-its-employees-sellers-and-consumers-where-is-the-harm/.

motivated to innovate by competitive threats like TikTok, a firm that didn't exist at the time of the purchase and whose effect could not have been predicted by regulators.

Further, the economic literature provides reason to consider the benefits of mergers and acquisitions. Bain & Company's Technology Report 2021 analyzed all acquisitions of $300 million or more, totaling $150 billion, by Alphabet, Amazon, Apple, Facebook (now Meta), and Microsoft from 2005 to 2020. Through a series of double-blinded case studies, Bain evaluated if an acquisition benefited consumers with lower prices, increased access to innovations, or improved already existent products or services. The study also gauged if the acquisitions increased competition by pressuring incumbents to innovate or by triggering more external investment. The report concludes that "most big tech M&A spending actually benefits consumers and doesn't hamper competition."[8]

More broadly, a presumption that acquisitions are harmful may have detrimental effects on the crucial cycle of funding start-ups and their innovations. A 2017 National Bureau of Economic Research (NBER) study, by Gordon M. Phillips of Dartmouth College and Alexei Zhdanov of the University of Lausanne, examined the relationship between venture capital (VC) activity and mergers and acquisitions globally across jurisdictions with different levels of regulatory permissiveness. They found "evidence of a strong positive association between VC investments and lagged M&A activity, consistent with the hypothesis that an active M&A market provides viable exit opportunities for VC companies and therefore incentivizes them to engage in more deals."[9]

Similarly, in a study published in May 2022, Tiago S. Prado and Johannes M. Bauer of Michigan State University studied the effects of 32,367 venture capital deals and 392 tech startup acquisitions by Google, Amazon, Apple, Facebook, and Microsoft from 2021 to 2020 on venture capital funding to emerging firms.[10] They conclude:

> Overall, we detected evidence of a positive, statistically significant increase in venture investment in the industry segments in which the acquired start-ups operate. During the ten-year period covered in our data, there are no detectable, systemic negative effects on start-up funding. Thus, the empirical evidence suggests that, in a given industry segment, venture capital resources available to start-ups for innovation purposes increase after big-tech acquisitions.[11]

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[8] David Crawford and Michael Schallehn, "Regulate with Care: The Case for Big Tech M&A," in *Technology Report 2021: The '20s Roar* (Bain & Company, 2021), pp. 14-23, https://www.bain.com/globalassets/noindex/2021/bain_report_technology-report-2021.pdf.

[9] Gordon M. Phillips and Alexei Zhdanov, "Venture Capital Investments and Merger and Acquisition Activity Around the World" (NBER Working Paper No. 24082, National Bureau of Economic Research, Cambridge, MA, November 2017), https://www.nber.org/papers/w24082.

[10] Tiago S. Prado and Johannes M. Bauer, "Big Tech Platform Acquisitions of Start-ups and Venture Capital Funding for Innovation," *Information Economics and Policy*, Vol. 59 (June 2022), https://www.sciencedirect.com/science/article/pii/S0167624522000129.

[11] Ibid, p. 15.

The discussion in the Draft Guidelines insufficiently considers the merits of and the motivations behind acquiring a firm. Axel Gautier and Joe Lamesch of the University of Liège studied 175 acquisitions made by Google, Amazon, Facebook, Amazon, and Microsoft (GAFAM) from 2015 to 2017. They concluded that these firms use acquisitions, for the most part, as a substitute for in-house R&D, since those acquisitions are intended to "strengthen their core market segments but rarely to expand their activities into new ones." They go on to observe that "most of the acquired products are shut down post acquisition, which suggests that GAFAM mainly acquire firm's assets (functionality, technology, talent or IP) to integrate them in to their ecosystem rather than the products and users themselves."[12] The draft Guidelines do not sufficiently recognize the motivations for acquisition. Neither do they acknowledge the potential advantages of acquisitions, including the possible benefits for workers or consumers.

Nor do the Guidelines support their assertion that internal "organic growth" is superior or favored by Congress.[13] That bias is a personal preference, not an economic or legal rationale, and should not be forced on others in the economy. More generally, a basic respect for property rights recommends a default of allowing owners to do with their property as they wish, unless a harm can be proven, not just conceived of as a possibility. The Guidelines suggest the opposite presumption in favoring internal growth over acquisition.

But perhaps the study's most illuminating finding involves so-called "killer acquisitions." Gautier and Lamesch define the term as an acquisition in the same core business as the buyer, continued operation under the original brand name, and having a substantial user base. Of the 175 transactions included in the study, only one qualified as a killer acquisition. While this is a narrower definition of "killer acquisition" than some use, it may be a more accurate and useful one. In any case, the low number of violations suggests purchasing to kill is not a widespread occurrence.

Similarly, Draft Guideline 6 lacks any discussion of the well-established benefits of vertical mergers. Once again, the draft quotes from the flawed economic thinking of *Brown Shoe v. United States*: "The primary vice of a vertical merger…is that, by foreclosing the competitors of either party from a segment of the market otherwise open to them, the arrangement may act as a clog on competition, which deprives rivals of a fair opportunity to compete."[14] But to place concern only on the plight of rivals is to miss the point of recent U.S. antitrust law. That point, as summarized by the Supreme Court in *Leegin Creative Leather Products, Inc. v. PSKS*, is to distinguish "between restraints with anticompetitive effect that are harmful to the consumer and restraints stimulating competition that are in the consumer's best interest."[15] The Court went on to contrast that distinction with the antithetical rationale of the provisions of state fair trade laws: "The rationales for these provisions are foreign to the Sherman Act. Divorced from competition and consumer welfare, they were designed to save inefficient small retailers from their inability

[12] Axel Gautier and Joe Lamesch, "Mergers in the Digital Economy" (CESifo Working Papers 8056 2020, January 2020), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3529012.
[13] Draft Merger Guidelines, p. 33.
[14] Draft Merger Guidelines, p. 17 (quoting *Brown Shoe Co. v. United States*, 370 U.S. 294, 323-24 (1962)).
[15] 551 U.S. 877, 886 (2007).

to compete."[16] The Guidelines betray the same faults: they are divorced from consumer welfare, which they never mention, and in the name of competition they seek to protect businesses from competition with larger rivals.

The significance of consumer welfare is reflected in a majority opinion by Justice Breyer that analyzed an agreement's effect on consumer welfare in determining that the FTC had stated a claim for violation of the Federal Trade Commission Act.[17] On this the dissent agreed: "The point of antitrust law is to encourage competitive markets to promote consumer welfare."[18] The Supreme Court has also taken consumer welfare into account in determining the coverage of the Robinson-Patman Act.[19] The Agencies' string citations to superseded cases do not absolve the Agencies of their obligation to discern and to follow the current state of the law.[20]

In particular, "the current understanding of section 7 is that it forbids mergers that are likely to 'hurt consumers, as by making it easier for the firms in the market to collude, expressly or tacitly, and thereby force price above or farther above the competitive level.'"[21] Not all mergers are likely to do that. It is a well-established economic fact that vertical mergers often benefit consumers with *lower* prices due to the elimination of double margins.[22] Also, it should not be taken as a given that foreclosure from self-dealing is anti-competitive. Courts have increasingly raised the amount of foreclosure needed to trigger alarm. That is because exclusive dealing can be a boon to competition if it promotes more effective distribution, minimizes free-riding, improves product quality, or provides a more reliable source of supply.[23] Former Director of the FTC's Bureau of Competition D. Bruce Hoffman wrote that "self-preferencing is likely to be beneficial to consumers and competition, or at worst harmless, except in certain particular circumstances."[24] To base evaluations of vertical mergers on structural factors is to miss a more nuanced and illuminating evaluation of the effects of any particular vertical merger; this is a disservice to consumers.

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[16] Ibid, p. 906.

[17] *F.T.C. v. Actavis, Inc.*, 570 U.S. 136, 154 (2013). This analysis is consistent with Judge Breyer's jurisprudence on the subject as a circuit judge. *E.g.*, *Grappone, Inc. v. Subaru of New England, Inc.*, 858 F.2d 792, 794 (1st Cir. 1988) ("[T]he antitrust laws protect the competitive process in order to help individual consumers by bringing them the benefits of low, economically efficient prices, efficient production methods, and innovation.").

[18] *F.T.C. v. Actavis, Inc.*, 570 U.S. at 161 (Roberts, C.J., dissenting).

[19] *Jefferson Cnty. Pharm. Ass'n, Inc. v. Abbott Labs.*, 460 U.S. 150, 158 n.17 (1983).

[20] The cases cited have an average date of 1982 and, when weighted for number of citations, 1975. Geoffrey Manne (@geoffmanne), "The average year of cases cited in the draft Merger Guidelines is 1982," X (formally Twitter), July 19, 2023, 2:08 p.m., https://twitter.com/geoffmanne/status/1681727830017839106?s=20.

[21] *United States v. Rockford Mem'l Corp.*, 898 F.2d 1278, 1282-83 (7th Cir. 1990) (quoting *Hosp. Corp. of Am. v. F.T.C.*, 807 F.2d 1381, 1386 (7th Cir. 1986).

[22] David Reiffen and Michael Vita, "Is There New Thinking on Vertical Mergers?," *Antitrust Law Journal*, Vol. 63, No. 3, pp. 920-921, https://www.jstor.org/stable/40843307.

[23] Jonathan M. Jacobson, "Exclusive Dealing, 'Foreclosure,' and Consumer Harm," *Antitrust Law Journal*, Vol. 70, No. 2 (January 2002), pp. 311-312, https://www.wsgr.com/a/web/179/jacobson_foreclosure.pdf.

[24] D. Bruce Hoffman and Garrett D. Shinn, "Self-Preferencing and Antitrust: Harmful Solutions for an Improbable Problem," *CPI Antitrust Chronicle* (June 2021), p. 3, https://www.clearygottlieb.com/-/media/files/cpi--hoffman--final-pdf.pdf.

Draft guidelines assume too much about a correlation between concentration and anticompetitive effects.

The Guidelines combine a disregard for efficiency with a superstition that concentration is detrimental to competitiveness. The kindest thing the Supreme Court has had to say about the notion that "Congress intended the courts to apply § 7 so as to keep small competitors in business at the expense of efficiency" was that it is "a proposition about which there is considerable disagreement."[25]

To presume that increased concentration is happening and is de facto detrimental to competitiveness is imprudent if not outrightly wrong. Yet Guideline 8 makes that very assumption. It states as much in its title: "Mergers Should Not Further a Trend Toward Concentration."[26] To assume concentration is always detrimental is a fundamental error.

This problem harkens back to the flawed 1948 FTC study that erroneously found increased concentration and accelerated rates of concentration in U.S. industry.[27] In a February 1950 article, John Lintner and Keith Butters disproved the conclusions of the FTC by highlighting the methodological flaws in the 1948 study.[28] The authors found that mergers were much more important to smaller rather than larger firms. Also, mergers actually reduced concentration by reducing shares among the biggest companies. Finally, Lintner and Butters found that merger activity among the biggest firms was minor and that their internal growth dwarfed the effects of mergers.[29] The economist authors of the FTC study would go on to admit their mistakes in a footnote by writing, "If the Commission had made any general statement on this point, it would probably have concluded, based on its data, that the recent mergers have not substantially increased concentration in manufacturing as a whole."[30]

Similar questions remain around the current state of concentration today. While many assume increasing concentration to be an established fact, there are contrary views. A March 2022 study by the U.S. Chamber of Commerce found that "industrial concentration has been declining rather than increasing," and that "concentration in the manufacturing sector and economy-wide concentration have both been declining since 2007." The study also finds that "average concentration in the U.S. economy declined by approximately two percent from 2007 to 2017."[31]

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[25] *Cargill, Inc. v. Montfort of Colo., Inc.*, 479 U.S. 104, 116 n.11 (1986).
[26] Draft Merger Guidelines, p. 21.
[27] Tim J. Muris, *Neo-Brandeisian Antitrust: Repeating History's Mistakes* (American Enterprise Institute, June 2023), p. 49, https://www.aei.org/research-products/report/neo-brandeisian-antitrust-repeating-historys-mistakes/.
[28] John Lintner and J. Keith Butters, "Effects of Mergers on Industrial Concentration, 1940-1947," *Review of Economics and Statistics*, Vol. 32, No. 1 (February 1950), https://www.jstor.org/stable/1928273.
[29] Muris, Neo-Brandeisian Antitrust, p. 49.
[30] Ibid, p. 50 (quoting Blair and Houghton, "The Lintner-Butters Analysis of the Effect of Mergers on Industrial Concentration," p. 67 n. 12).
[31] "U.S. Chamber Study: Industrial Concentration in the U.S. Economy Is Declining, Not Increasing," U.S. Chamber of Commerce, March 9, 2022, https://www.uschamber.com/finance/antitrust/u-s-chamber-study-industrial-concentration-in-the-u-s-economy-is-declining-not-increasing.

Relatedly, the assumption that an increase in concentration is always a detriment to competition is incorrect. Industrial organization economists have long known that changes in market concentration can both increase or decrease competition in that market.[32] In fact, the Chamber of Commerce study found that "[r]ising industrial concentration is often a sign of increasing market competition and associated with positive outcomes such as output growth, job creation, and higher employee compensation."[33]

Similarly, a recent report from the International Center for Law and Economics notes the perils of focusing solely on national concentration trends over local trends, where competition actually takes place. They explain that increasing national-level firm concentration drives increased competition and decreased concentration in local markets. They also highlight the increased significance for consumers in local markets, rather than national ones. They write, "Rising national concentration, where it is observed, is a result of increased productivity and competition that weed out less-efficient producers. Similar results hold for labor-market effects."[34]

The authors go on to quote former Clinton-era deputy assistant attorney general for economics at the DOJ's Antitrust Division:

> [S]imply as a matter of measurement, the Economic Census data that are being used to measure trends in concentration do not allow one to measure concentration in relevant antitrust markets, i.e., for the products and locations over which competition actually occurs. As a result, it is far from clear that the reported changes in concentration over time are informative regarding changes in competition over time.[35]

Regardless of the amount of concentration, the rate at which it may or may not be increasing, and the proper markets in which to look for trends, it is a well-accepted fact among economists that one cannot prove a causal relationship between concentration and market outcomes.

A paper by assistant attorney general for economics in the DOJ Antitrust Division under President Obama, Fiona Scott Morton, former director of the FTC Bureau of Economics under President Obama, Martin Gaynor, and Steven Berry shows bipartisan agreement on the underlying economics of correctly evaluating the consequences of concentration. They write, "our own view, based on the well-established mainstream wisdom in the field of industrial

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[32] Joshua D. Wright, *Towards a Better Understanding of Concentration: Measuring Merger Policy Effectiveness* (Note submitted as background material for OECD Hearing on Market Concentration, DAF/COMP/WD(2018)69, June 6, 2018), p. 2, https://one.oecd.org/document/DAF/COMP/WD(2018)69/en/pdf.
[33] "Industrial Concentration in the U.S. Economy is Declining," U.S. Chamber of Commerce.
[34] Geoffrey Manne et al., Comments of the International Center of Law and Economics on Request of Information on Merger Enforcement, Docket No. FTC-2022-0003-0001, April 21, 2022, p. 10, https://laweconcenter.org/wp-content/uploads/2022/04/ICLE-Comments-on-Merger-Enforcement-RFI-April-2022.pdf.
[35] Gregory J. Werden and Luke M. Froeb, "Don't Panic: A Guide to Claims of Increasing Concentration," *Antitrust*, Vol. 33, No. 1 (Fall 2018), p.74.

organization for several decades, is that regressions of market outcomes on measures of industry structure like the Herfindahl-Hirschman Index should be given little weight in policy debates."[36]

But Draft Guideline 1 ignores that economically sound advice by increasing the weight put on the Herfindahl-Hirschman Index and by lowering the threshold for triggering scrutiny by the agencies. The Guideline states that a market will be considered "highly concentrated" if the post-merger HHI score is greater than 1,800, the change in HHI is 100 points or more, or it creates a firm with more than thirty percent market share. By narrowing the evaluative process to a more rigid structural analysis and placing less emphasis on actual effects of a merger, the Agencies risk over-deterrence of procompetitive mergers. This risks real losses to consumers of lower prices, innovations, and prosperity.

As former FTC Chair Tim Muris and former FTC Director of the Bureau of Economics Bruce Kobayashi explain in a recent paper for the Competitive Enterprise Institute:

> Prospective merger screening at the federal antitrust agencies has evolved, using advances in theoretical and empirical economics, to deemphasize structural tests in favor of an effects-based analysis. The agencies' merger guidelines have changed with this evolution in economic knowledge and agency practice. The goal of guideline changes has been to increase the predictability and accuracy of the agencies' merger screening, thereby decreasing the social costs of merger enforcement.[37]

The Agencies should use the best tools and empirical evidence in merger enforcement instead of over-emphasizing structural factors. The present draft of the Merger Guidelines would increase the costs of interventions without improving the success of the results. This is a disservice to the taxpayer, to the consumer, and to the U.S. economy at large. The agencies should reconsider this approach to avoid harmful Type I errors of enforcement.

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[36] Steven Berry, Martin Gaynor, and Fiona Scott Morton, "Do Increasing Markups Matter? Lessons from Empirical Industrial Organization," *Journal of Economic Perspectives*, Vol. 33, No. 3 (Summer 2019), p. 48, https://pubs.aeaweb.org/doi/pdfplus/10.1257/jep.33.3.44; see also Jonathan Baker and Timothy Bresnahan, "Economic Evidence in Antitrust: Defining Markets and Measuring Market Power" (Working Paper No. 328, John M. Olin Program in Law and Economics, Stanford Law School, September 2006) ("The Chicago identification argument has carried the day, and structure-conduct performance empirical methods have largely been discarded in economics.").

[37] Bruce H. Kobayashi and Timothy J. Muris, *Turning Back the Clock: Structural Presumptions in Merger Analyses and Revised Merger Guidelines*, Competitive Enterprise Institute, February 22, 2023, p. 2, https://cei.org/studies/turning-back-the-clock-structural-presumptions-in-merger-analyses-and-revised-merger-guidelines/.

Conclusion

The Draft Merger Guidelines are flawed with a presumption of harm directed at too many mergers, a lack of rigorous economic analysis, an absence of concern for consumer welfare, and an incomplete picture of case law. They should not be adopted as final guidance.

Respectfully,

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