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Expert Analysis

FTC Study Signals Fresh Changes To Merger Remedy Negotiations

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In September 2014, Chairwoman Edith Ramirez of the Federal Trade Commission championed a fresh study of merger remedies to update the commission's "very useful" review of divestitures undertaken in the late 1990s.[1] On Jan. 9, 2015, the commission made good on Ramirez's suggestion by releasing a new proposal for the retrospective study of merger remedy orders from 2006 to 2012.[2]

As Ramirez and antitrust scholars have noted,[3] retrospective studies of merger remedies inform and shape the development of competition policy. These studies provide a wealth of information to the conducting agency, but also give businesses the crucial opportunity to interact informally with agencies as the agencies look to identify the market trends that will inform future policy. Many businesses willingly participated in the commission's 1990s study and, as a result helped, shape the commission's reassessment of its divestiture process. Companies have that same opportunity once again.

As businesses participate in the proposed study to have input in the commission's thought process, they should also be aware of the historical link between retrospective merger remedy studies and substantial changes to commission policies. The commission's 1990s study coincided with significant shifts to its standard merger remedy negotiation practices. The new study's expanded scope, well beyond what the commission undertook in the 1990s, suggests that the commission may this time be considering changes beyond just the divestiture process. This dynamic policy environment increases the value that practitioners and market participants can bring through participation.

The 1990s Study

In 1999, the commission released the results of a comprehensive multi-year review of 35 divestiture orders it issued from 1990 to 1994 that forced the sale of tangible assets or intellectual property to remedy anticompetitive effects resulting from a merger or acquisition. In the divestiture process, merging parties and commission staff negotiate the terms of the remedy needed to gain approval of the transaction, resulting in a consent agreement. Remedies range from behavioral commitments to asset divestitures.

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In the 1999 study, the commission used a "case study" methodology: It interviewed divestiture buyers and issued qualitative and limited quantitative findings based on the results, compiling conclusions from the interviews after analysis. The 1999 study concluded at the outset that divestitures were appropriate remedy mechanisms that created viable competitors in markets of concern.[4] Following the path set forth by this initial conclusion, the study was relatively narrow and focused on examining the mechanics of procedures surrounding the commission's divestiture orders.

The core substantive finding of the 1999 study was that a fundamental "informational and bargaining imbalance" existed between merging companies on the one hand and the commission's staff and divestiture buyers on the other.[5] Participating divestiture buyers told the commission that they had much less bargaining power than divesting parties and that they often traded away the position of strength a divestiture order provided out of fear of alternative buyers or because of a lack of knowledge about the economics of the assets they were buying.[6] As a result of these issues, merging companies often proposed narrow divestiture asset packages, urged weak buyers, and neglected to-be-divested assets, while buyers negotiated disadvantageous deals, seemingly against self-interest, and then did not report difficulties to the commission.[7]

These findings in turn justified ongoing changes to how the commission was approaching divestitures. In the late 1980s and early 1990s, the commission had assumed that divestiture buyers and merging companies had roughly equivalent bargaining power. Despite the merging companies' superior information about the to-be-divested assets, the commission felt that buyers' countervailing status as bidders in compulsory sales corrected any bargaining asymmetry. So firmly did the commission hold this belief that it structured the divestiture process around it, regularly accepting proposals proffered by merging companies and divestiture buyers because of the assumption that they were the products of free and fair market bargaining.[8]

In the early- to mid-1990s, the staff of the Bureau of Competition at the commission began detecting issues with the markets resulting from divestiture proposals that had received commission approval simply because they had been negotiated by a willing buyer and seller.[9] Assistant Attorney General William Baer, then the Director of the commission's Bureau of Competition, confirmed that these issues were the impetus for the 1999 study.[10] Unsurprisingly then, the 1999 study ended up offering the necessary justification for the commission to alter its preexisting beliefs and practices.

Holding up the 1999 study's findings as evidence, the commission continued its new mid-1990s practice of demanding stricter terms in divestiture orders in order to correct the bargaining imbalance that it identified between buyers and sellers.[11] Specifically, these changes included shortening the length of the standard divestiture period from 12 months to six or fewer months, consistently requiring up-front buyers in cases involving select asset divestitures instead of full

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business line divestitures, and requiring monitors more frequently, particularly in the pharmaceutical and technology industries.[12] All of these shifts were tied to the study the commission conducted in the 1990s, and all ended up having signal importance for attorneys advising clients on all sides of divestiture equations.

The 2015 Proposal

The commission's Jan. 9 proposal for a new study is much loftier in both methodological and substantive ambition than its predecessor was. The new study would be a more resource-intensive and comprehensive review of commission merger policy than the 1999 study and would look to build on the conclusions of the 1999 study to derive new lessons for the future.

The broadened methodological scope of the proposed study is clear. The Jan. 9 proposal calls for review and analysis of 92 commission merger remedy orders issued from 2006 to 2012, as opposed to the 35 orders from a shorter time frame reviewed in the 1999 study.[13] The new proposal calls for review of 53 of these 92 commission orders using the same "case study" methodology as 1999. However, in these 53 long form case studies the commission plans to interview both buyers and, in a new development, an average of two customers and two competitors in each affected market.[14] And although the commission proposes abbreviated methodologies for other orders in industries such as supermarkets, drug stores, funeral homes, hospitals, and pharmaceuticals in which it has expertise, the commission's knowledge of those industries is the result of years of monitoring and information collection that generate as much or more data to back conclusions than interviews alone.

In perhaps the most significant methodological departure from the 1999 study, the commission plans to seek voluntary interviews in the first instance, but makes clear that it may rely on compulsory process to obtain information that it may need for the new study where necessary. The commission indicates that it will seek annual unit and dollar sales data for the year of the remedy and the three immediately preceding and following years from as many as 280 study participants.[15] By releasing a proposal containing the possibility of such data requests, the commission shows awareness of the tradeoff between the potential burden on unwilling or unable study participants and the need for maximum information in order to support clear recommendations and action. The commission's decision to float the possible use of compulsory process underscores its clear intent to rest any new findings on firm footing.

The widened substantive scope of the new proposal also is clear. By proposing to interview a wider range of market participants than just divestiture buyers—as it did last time around—the commission shows a willingness to assess not just the processes surrounding the negotiation of divestitures, but also the broader question of "whether the Commission's orders achieved their remedial goals."[16] Moreover, the new proposal calls for review not just of the effectiveness of merger remedies, but also of procedural issues raised by changes in merger remedy negotiation practices that coincided with the 1999 study.

Historical Context

Given its elevated ambition compared to the 1999 study, as well as the significant divestiture policy changes that coincided with the 1999 study, the 2015 proposal could be a harbinger of even more significant modifications to come in the commission's approach to negotiating merger remedies.

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The new proposal signals the commission's desire to reevaluate not just the form of the divestiture process, but also the substantive effectiveness of the remedies that it currently seeks. The 1999 study could not fully support such a substantive reevaluation, in part because it was based largely on interviews with divestiture buyers and so was only able to produce actionable insights into the disadvantages buyers faced and the procedural fixes the commission could implement. In contrast, the new study calls for interviews of buyers, sellers, competitors, and other market participants. Such multifaceted interviews could produce a new understanding, for example, of the kinds of industry characteristics or market structures that facilitate the effectiveness of one type of remedy over another, or the divestiture of one kind of asset over another. A better grasp of why a specific remedy succeeds or fails in a particular industry or market structure could conceivably lead to important changes in the types of remedy the commission is willing to seek in any given circumstance.

Of course, the exact contours of these changes, and particularly of the changes that become standard practice at the commission, are likely to depend heavily on the findings of a study that was proposed less than a month ago and that, judging from previous efforts, will likely take years to complete. The specific industries in which the study will have the most impact also are not obvious. As in 1999, certain industries could be in for larger changes than others when it comes to remedy negotiations. For example, the technology and pharmaceutical industries have become used to monitors since the 1990s, a suggestion included in the 1999 study.

Even though any changes to the commission's remedy policies will take time to come into focus, the commission did begin seeking stricter divestiture terms prior to the release of its 1999 study and had essentially identified the concerns addressed by the 1999 study prior to 1999. If history is a guide, commission staff may have already identified anecdotal concerns supporting the authorization of the study and such concerns may figure in individual merger remedies negotiations in a much shorter time frame. To lend guidance and certainty to practitioners and market participants, as results of the proposed study come in, the commission's Bureau of Competition should engage in a public dialogue that would allow it to update the 2012 Statement on Negotiating Merger Remedies. The 2012 guidelines are a useful guide to those faced with a divestiture negotiation, and an update following a study as wide-ranging and potentially transformative as this could bring the added clarity that is in everyone's interest.

Conclusion

Changes in how the commission negotiates merger remedies are possible in the wake of its ambitious proposed study, which will undoubtedly uncover new evidence about what contributes to remedy success or failure. Practitioners should stay attuned to impending developments, and interested businesses have the incentive to participate and lend their voices to what will be a thorough and careful process that could result in significant policy changes that may affect them. Those wishing to submit comments on the underlying study framework must submit by March 17.

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4. William J. Baer, Director, Bureau of Competition of the Federal Trade Commission, A Study of the Commission's Divestiture Process (Public Version), http://www.ftc.gov/sites/default/files/attachments/merger-review/divestiture.pdf, at 8 (1999).
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7. Id. at 16-27.
8. Id. at 16.
9. William Baer and Ronald Redcay, "Solving Competition Problems in Merger Control: The Requirements for an Effective Divestiture Remedy," 69 Geo. Wash. L. Rev. 915, 919 (2001).
10. Id. at 920.
11. See Baer, supra note 4, at iv, v.
12. Id. at 39-42.
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14. Id. at 2424.
15. Id.
16. Id.