

Market Definition And Implications For Merger Review

Law360, New York (July 11, 2011) -- While the 2010 Horizontal Merger Guidelines de-emphasize market definition analysis and place an increased focus on competitive effects, market definition continues to be central to establishing a prima facie case in court. This dissonance means that, despite the importance of focusing on the ultimate effect of a proposed transaction on consumers and competition, the antitrust enforcement agencies must continue to pay considerable attention to relevant market definition, particularly if they anticipate the need to challenge the transaction in court.

Indeed, recently litigated merger cases suggest that the U.S. Federal Trade Commission and U.S. Department of Justice are more likely to prevail in court when they are able to successfully defend their proposed market definition (in addition to demonstrating likely anti-competitive effects).

Thus, despite the new Merger Guidelines, the FTC and DOJ will need to continue to pay a great deal of attention to market definition (and the evidence that supports it) during the merger review process. Practitioners, in turn, should do the same.

The De-Emphasis on Market Definition in the Merger Guidelines

The 2010 Merger Guidelines state that “market definition helps specify the line of commerce and section of the country in which the competitive concern arises.” Dep’t of Justice and Fed. Trade Comm’n, Horizontal Merger Guidelines, at 7 (Aug. 19, 2010) [hereinafter “2010 Merger Guidelines”]. They further indicate that market definition “allows the agencies to identify market participants and measure market shares and market concentration.” *Id.*

The 2010 Merger Guidelines also make clear, however, that “the measurement of market shares and market concentration is not an end in itself.” *Id.* Instead, such measurement “is useful to the extent it illuminates the merger’s likely competitive effects.” *Id.*

In contrast, the 1992 Merger Guidelines (which were revised in 1997) treated market definition as a foundational element of a merger investigation: “First, the gency assesses whether the merger would significantly increase concentration and result in a concentrated market, properly defined and measured.” Dep’t of Justice and Fed. Trade Comm’n, Horizontal Merger Guidelines at 3 (revised April 8, 1997).

Thus, the 2010 Merger Guidelines demonstrate a shift in priority. They make clear that the agencies “need not start with market definition.” They also blur the line between competitive effects and market definition. See *id.* (“Evidence of competitive effects can inform market definition just as evidence of market definition can be informative regarding competitive effects.”).

Indeed, the 2010 Merger Guidelines now suggest that evidence of a likely price increase caused by a reduction in the number of rivals may “directly predict the competitive effects of a merger, reducing the role of inferences from market definition and market shares.” *Id.*

According to the agencies, the 2010 Merger Guidelines’ shift away from market definition as a foundational element is reflective of already-existing agency practice. While this approach might summarize agency practice, it does not reflect the emphasis that the courts are placing on market definition.

Market Definition in the Courts

Indeed, the courts still give great weight to evidence and arguments pertaining to market definition. For instance, in two preliminary injunction hearings litigated by the FTC in 2011 — and the first two merger litigations that have been tried since the 2010 Merger Guidelines were issued — the courts paid considerable attention to the agencies’ proposed market definitions in deciding whether to grant the preliminary injunction.

In *FTC v. ProMedica Health System Inc.* (N.D. Ohio Mar. 29, 2011), the merging parties accepted the FTC’s proposed market definition, from which Judge David Katz concluded that the merging parties had high market shares in a highly concentrated market. *Id.* at *10-12.

This finding was central to the court’s conclusion that the FTC had established a *prima facie* case that the proposed transaction would be anti-competitive. *Id.* at *12 (“[T]he acquisition is presumptively anticompetitive in both relevant markets based on these high levels of market concentration, [sic] and is presumed likely to enhance ProMedica’s market power in both markets.”).

In *FTC v. Laboratory Corporation of America*, No. SACV 10:1873 AG, Dkt. No. 128 ¶ 157 (C.D. Cal. Feb. 22, 2011) [hereinafter “LabCorp”], the merging parties did not concede the relevant market, and Judge Andrew Guilford devoted a considerable portion of his decision to assessing the FTC’s proposed geographic and product markets. *Id.* ¶ 157. Judge Guilford ultimately ruled that the evidence did not establish that the FTC was likely to succeed on the merits. *Id.* ¶ 167 (“[T]he court cannot conclude at this time that the FTC has demonstrated likelihood of success on the merits.”).

Those courts’ emphasis on market definition stemmed in part from the large body of pre-existing case law, which makes clear that market definition is a key aspect of a *prima facie* case. Notable examples are the decisions in *Whole Foods*, *Staples* and *Oracle*.

See *FTC v. Whole Foods Mkt. Inc.*, 548 F.3d 1028, 1036 (D.C. Cir. 2008) (“The FTC contends the district court abused its discretion ... by treating market definition as a threshold issue ... [But we hold that] [t]he district court acted reasonably in focusing on the market definition.”); *FTC v. Staples Inc.*, 970 F. Supp. 1066, 1073 (D.D.C. 1997) (“As with many antitrust cases, the definition of the relevant product market in this case is crucial.”); *United States v. Oracle*, 331 F. Supp. 2d 1098, 1110 (N.D. Cal. 2004) (“In determining whether a transaction will create or enhance market power, courts historically have first defined the relevant product ... a ‘necessary predicate’ to finding anticompetitive effects.”).

Because of those and other cases, a court would have to go against precedent and side with untested regulatory guidance to conclude that relevant market definition analysis may be minimized or set aside entirely. In turn, the FTC and DOJ would be taking a big litigation risk if they were to abandon market definition when pleading their case to a federal court. As a consequence, the antitrust agencies are essentially forced to put forth evidence that supports both their proposed market definition and their

arguments about the likely competitive effects of the transaction even where they believe they have sufficient proof of the latter.

In trying to bring evidence to bear on market definition, empirical analyses of consumer demand and customer switching data can be useful. In addition, the antitrust agencies often rely on customer testimony and corresponding analysis from an economic expert analyzing what that testimony means with regard to how customers might react to a small but significant and nontransitory increase in price (“SSNIP”).

However, while declarations from customers may influence the agencies’ view of the relevant market and the competitive effects of the proposed transaction, the courts typically consider such testimony in conjunction with (and as tempered by) other empirical evidence.

For example, in *Oracle*, Judge Vaughn Walker of the Northern District of California looked to empirical evidence on competitive effects and entry to inform his analysis of the relevant market. 331 F. Supp. 2d at 1123 (“Market definitions, statistical presumptions and likelihood of unilateral anticompetitive effects are all issues on which the parties contended vigorously and presented much evidence.”).

Thus, while customer testimony is important generally, courts have not viewed it as definitive evidence for the purpose of antitrust market definition. Indeed, courts have ignored or downplayed customer testimony regarding how customers would respond to a hypothetical SSNIP where other empirical evidence was available. See *Staples*, 970 F. Supp. at 1076-86 (considering competitor testimony when analyzing new entry but statistical price data when analyzing market definition and competitive effects).

Implications for Merger Review

Ultimately, what happens in the courts must guide the type of analysis that is done in a merger evaluation. Market definition is, thus, still important because courts continue to look to the antitrust agencies to define and defend a relevant market in which the market shares and concentration are sufficient to help support a prima facie case.

Accordingly, the FTC and DOJ must continue to focus on market definition in the merger review process, and perhaps more than what the 2010 Merger Guidelines may suggest. To do otherwise would compromise the agencies’ ability to bring successful actions in court.

Practitioners also should recognize that market definition continues to be an important part of the merger review process. To that end, practitioners need to keep in mind the types of evidence and arguments that the courts find valuable and persuasive, even if the agencies might not give such evidence and arguments as much weight during the merger review process.

--By Corey Roush, Hogan Lovells LLP, and Lawrence Wu (pictured), NERA Economic Consulting

Corey Roush is a partner in the Washington, D.C., office of Hogan Lovells. Lawrence Wu is a senior vice president in the San Francisco office of NERA Economic Consulting. Both represented Laboratory Corporation of America in the recent merger case brought by the FTC, which is referenced in this article.

The opinions expressed are those of the authors and do not necessarily reflect the views of the firm, its clients, or Portfolio Media, publisher of Law360. This article is for general information purposes and is not intended to be and should not be taken as legal advice.

