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Recent Developments

U.S. Antitrust Agencies Unveil Proposed New Horizontal Merger Guidelines

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On April 20, 2010, the Federal Trade Commission released for public comment a proposed new version of the Horizontal Merger Guidelines. The Guidelines outline how the FTC and the Justice Department evaluate the likely competitive impact of mergers involving actual or potential competitors and determine whether to challenge those mergers. The antitrust agencies propose to update the Guidelines—largely unchanged since 1992—to reflect their current enforcement approach more accurately.[1] The FTC will accept public comments on the proposal until June 4, 2010.

The proposed new Guidelines clarify parts of the agencies' analytical policies, address several new concepts, provide illustrative examples, and revise concentration thresholds, including:

- A clear statement that the agencies view market definition as not an end in itself or even a necessary starting point of merger analysis, but merely as a useful tool to the extent it illuminates a merger's likely competitive effects—an approach at odds with prevailing case law.
- An updated explanation of the tests used to define relevant antitrust markets, including more detailed methods for applying the traditional "hypothetical monopolist" test to product and geographic markets, and a new discussion of "critical loss analysis"—a market definition test that requires detailed cost, profitability, and demand data.
- A significantly revised and expanded treatment of unilateral competitive effects theories in mergers involving bidding markets, innovation markets, and branded product markets—stressing the use of alternative competitive effects tests rather than traditional market definition and concentration analysis.
- Relaxed market concentration "safe harbor" thresholds, based on the Herfindahl-Hirschman Index, in transactions where traditional market definition concepts still apply.
- A new section on "Targeted Customers and Price Discrimination," setting out the necessary conditions for showing competitive harm to customers who are vulnerable to selective price discrimination by suppliers.
- Removal of specific time frames relevant to considering supply responses by current competitors and *de novo* entrants.
- Brief new sections on the relevance of powerful buyers, the potential for mergers between rival purchasers to create monopsony power, and competitive analysis of minority equity investments.

Notwithstanding all those changes, the agencies do not propose to relax the requirements of the "failing firm" defense for mergers, despite criticisms that the defense's rigidity is incompatible with the urgent needs of failing firms and banks in the current economic climate.

Some of the proposed Guidelines' new theories will face hurdles in the federal courts. Indeed, in a very recent decision, *City of New York* v. *Group Health Inc.*, a district court dismissed the City's antitrust challenge to a previously consummated merger between two health insurers, finding the City's alleged product market allegation inadequate as a matter of law. The court concluded that the City had asserted a market in which the City was the only customer and the merging parties were the principal suppliers. Narrow as this alleged market was, it might have found support in the proposed Merger Guidelines, which extensively discuss markets consisting of targeted subsets of customers to whom merging parties can selectively raise prices (so-called "price discrimination" markets). And

1 *See* http://www.ftc.gov/os/2010/04/100420hmg.pdf.

contrary to the district court's holding, the proposed Guidelines state that it may be valid to define markets "that are as narrow as individual customers."[2]

The district court also thwarted the City's attempt to assert an "upward pricing pressure" (or "UPP") test as an alternative to product market definition. The UPP test—which is among the new theories endorsed by the proposed Merger Guidelines—dispenses with market definition and purports to analyze directly whether a merger will incentivize price increases. The district court noted, however, that

> its research has not revealed a single decision of a federal court adopting this test. In light of the case law's clear requirement that a Plaintiff allege a particular product market in which competition will be impaired, the absence of authority is hardly surprising.[3]

Assuming the district court's decision withstands appeal, that statement underscores the challenges posed by prevailing case law to the antitrust agencies' attempts to assert competitive effects theories that forego traditional antitrust market definition.

The agencies characterize their proposed new Guidelines as more descriptive than prescriptive, claiming they better reflect how the FTC and Justice Department currently conduct merger reviews. But the proposal heralds significant changes in its emphasis on alternative competitive effects analyses (*e.g.*, critical loss, upward pricing pressure) and the diminished role for traditional market definition and concentration measurements. Assuming this more open-ended approach to merger analysis is codified in a final version of the new Guidelines, it may lead to more challenged mergers or increased demands for divestiture remedies. It also remains to be seen whether these Guidelines, with their reliance on tests requiring more detailed data and evidence, will imperil rather than facilitate predictability and speed in merger review.

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2 Id. at § 4.1.4.

3 *City of New York* v. *Group Health Inc*., No. 06 Civ. 13122 (RJS), at 7 n.6 (S.D.N.Y. May 11, 2010).

SEC Agrees to Reduce Penalties in Exchange for Cooperation

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In two recent insider trading actions, the SEC agreed to settlements with substantially reduced civil penalties based on the defendant's agreement to cooperate with an ongoing investigation and related enforcement action. *SEC* v. *Cutillo et al.*, No. 09 Civ. 9208 (S.D.N.Y. Mar. 30, 2010); *SEC* v. *Galleon Management, LP et al.*, No. 09 Civ. 8811 (S.D.N.Y. Apr. 19, 2010). These cases merit attention as the SEC reportedly considers revising its framework for assessing penalties against entities.

The Commission brought these two actions against Schottenfeld Group LLC—a registered broker-dealer—based on alleged insider trading by individuals who, at the time of the trading, were registered representatives and proprietary traders at Schottenfeld. The SEC is statutorily authorized to obtain civil penalties of up to three times the profit gained or loss avoided as a result of insider trading. Historically, the Commission's practice in insider trading settlements has been to secure a "one-time" penalty equal to the amount of disgorgement.

In the *Cutillo* and *Galleon* actions, however, the Commission submitted and the courts approved settlements that included civil penalties equal to only 50% of the disgorgement amounts. In a joint submission to the court in *Galleon,* the parties explained that the penalty in that case represented a 50% "discount from a one-time penalty, in exchange for [Schottenfeld's] agreement to cooperate with the Commission." The final judgments in both cases stated that penalties in excess of the amounts agreed were not being ordered "based on Defendant's agreement to cooperate in a Commission investigation and related enforcement action." While this is not stated explicitly in the filings, the settlements suggest that Schottenfeld may have entered into a formal cooperation agreement, as contemplated by the initiatives announced by the SEC in January. It is also unclear whether the settlements are based on the defendant's forward-looking promise to cooperate or, rather, are based in whole or in part on cooperation that has already occurred.

