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A Busy Year in U.S. M&A Antitrust Enforcement

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As M&A activity reached an unprecedented level in 2015, the U.S. antitrust agencies continued to actively investigate and pursue enforcement actions impacting transactions in many sectors of the economy. The overall level of merger enforcement was roughly in line with the aggressive levels of the past few years, with the Federal Trade Commission and the Department of Justice on a combined basis initiating court challenges to block seven proposed deals and requiring remedies in 23 more. In addition, companies abandoned four transactions due to opposition from the antitrust agencies.

Court Challenges

The past year saw some notable court challenges, confirming that the agencies remain willing to litigate to block proposed deals. In July 2015, the DOJ challenged Electrolux's proposed acquisition of General Electric's appliance business. The DOJ's complaint alleged that the transaction would combine two of the three leading manufacturers of cooking appliances and would create a duopoly between Electrolux and Whirlpool in the supply of cooking appliances to "home builders, property managers, and other contract-channel appliance purchasers." According to the DOJ complaint, few suppliers can meet the demands of this customer group, which include having a full line of kitchen appliances, a variety of choices and models, and a large and sophisticated distribution network. In early December, after five months of litigation and four weeks into the trial, GE exercised its option toabandon the transaction and collect a $175 million termination fee.

The FTC also had a busy litigation docket, including two preliminary injunction trials in federal court, winning one and losing the other, and four other litigations pending resolution. In June, the agency prevailed in a suit to enjoin Sysco Corporation's acquisition of US Foods. The FTC alleged a narrow market for broadline food distribution to national customers, based on a theory of customer discrimination, and asserted that the companies are the only two broadline food distributors with nationwide networks of distribution centers. In its opinion, the U.S. District Court for the District of Columbia adopted the FTC's market definition and concluded that the merger would have eliminated head-to-head competition between the country's two largest competitors in the market for national customers.

In contrast, the FTC lost its challenge of the proposed merger of Steris Corporation and Synergy Health. As discussed in our memo, the FTC did not allege that the transaction would eliminate

existing competition between the parties. Instead, the FTC relied on the so-called "actual potential entrant" doctrine, arguing that, but for the merger, Synergy would have entered the U.S. market with X-ray sterilization technology. The U.S. District Court for the Northern District of Ohio disagreed, finding that while Synergy considered the possibility of bringing X-ray sterilization to the U.S., it never overcame the business and financial hurdles inherent to that strategy, including securing customer commitments and reducing the capital costs associated with the project. The court held that the evidence showed "unequivocally" that Synergy's failure to obtain customer commitments and to lower capital costs "plagued the development of X-ray sterilization" and was the cause of Synergy's termination of the project.

Just a few weeks ago, the FTC sued to block the proposed merger of Staples with Office Depot (see our post earlier this month). In 1997, the FTC successfully sued to block the two office supplies retailers' first attempt to combine, alleging that "office superstores" constituted a distinct relevant market. While in 1997 the FTC alleged competitive harm in the sale of office supplies to consumers and small businesses, the recent complaint alleges a theory of competitive harm similar to that pursued in the *Sysco* litigation. The FTC's case limits the alleged market to direct sales of office supplies "to large business-to-business customers," with a focus on customers that "have nationwide or multiregional operations and require an office supplies vendor that can provide low pricing, high levels of service, and delivery across all of their operations." The preliminary injunction trial is scheduled to begin in March 2016. In addition, the FTC recently brought suits in federal court to block three proposed hospital mergers, including the merger of Advocate Health Care and North Shore University Health System in Chicago, Penn State Hershey Medical Center's merger with Pinnacle Health System in Harrisburg, Pennsylvania, and Cabell Huntington Hospital's acquisition of St. Mary's Medical Center in Huntington, West Virginia.

Abandoned Transactions

Other transactions facing opposition from the antitrust agencies were abandoned by the parties before a court challenge. In April, over 15 months after Comcast proposed acquiring Time Warner Cable, the parties abandoned the transaction due to the FCC's and DOJ's "significant concerns that the merger would make Comcast an unavoidable geographic overlap between the parties, the agencies were concerned that Comcast, as a result of its "dominant" share of high-speed broadband customers—reportedly 57% nationwide—and programming ownership, would have both the ability and incentive to harm online video distributors. Also in April, and again following a lengthy DOJ investigation, Applied Materials and Tokyo Electron abandoned their merger plans after the DOJ informed them that their remedy proposal failed to resolve the competitive concerns. Applied Material and Tokyo Electron, respectively the first and third largest competitors in the semiconductor equipment industry, make an assortment of machines used for fabricating computer chips, some of which carry out similar functions. While the parties apparently offered to divest the overlapping business lines of Tokyo Electron, the DOJ reportedly focused on the impact of the deal on innovation, expressing concerns that the merger would combine two large competitors with the necessary know-how, resources, and ability to develop new semiconductor manufacturing equipment. Most recently, in early December, the DOJ announcedthat Chicken of the Sea and Bumble Bee Foods, the second and third largest sellers of shelf-stable tuna in the U.S., had abandoned their merger plans due to the DOJ's serious competitive concerns.

Difficult Deals Still Getting Through

In a year of vigorous antitrust enforcement, a number of difficult transactions were approved either unconditionally or with remedies. In September, the DOJ announced that it would not challenge Expedia's acquisition of Orbitz, a transaction that faced significant opposition from the hotel industry. The DOJ found that the acquisition was unlikely to harm competition because Orbitz only constitutes a small source of bookings for hotels, airlines and car rental companies, and the online travel business is rapidly evolving with several new services being launched to compete with the existing providers. In February, the FTC approved Zillow's proposed acquisition of Trulia, respectively the first and second largest web portals for home buying that sell advertising space to real estate agents. Although the parties' internal documents showed that "Zillow and Trulia compete closely with one another for consumer traffic and for real estate agent advertising dollars," the evidence also showed that real estate agents use numerous methods in addition to the parties' platforms to attract customers. The FTC found insufficient evidence that real estate agents would face higher prices post-merger, or that the combined company would have a reduced incentive to innovate.

Most enforcement actions in 2015 were resolved through consent orders requiring remedial action. Notable cases include Dollar Tree's acquisition of Family Dollar Stores and the merger of RJ Reynolds and Lorillard. In *Dollar Tree*, the FTC asserted that the two chains competed head-to-head in terms of price, product assortment and quality as well as location and customer service in local markets across the country. The agency required divestiture of 330 Family Dollar stores to resolve competitive concerns. The FTC's clearance of the merger of Reynolds and Lorillard, respectively the second and third largest U.S. cigarette manufacturers, was subject to the divestiture of four cigarette brands to Imperial Tobacco. The FTC alleged that, absent the divestiture, the merger would have raised significant concerns by eliminating current and emerging head-to-head competition between the parties in the highly concentrated cigarette market, thereby increasing the chances of unilateral price hikes as well as coordinated interaction between Reynolds and Altria, the industry leader.

Enforcement Trends and Issues

Enforcement activity in 2015 shows that the FTC and DOJ are prepared to pursue aggressive theories with respect to market definition and competitive effects. In a number of cases, the agencies defined product markets based on narrow customer groups that purportedly have different requirements that only a few suppliers can satisfy and that may be vulnerable to discriminatory treatment. This approach substantially limits the number of competitors that the agency counts as being in the relevant market and increases the competitive significance of the merging parties, thereby supporting a claim of competitive harm. The agencies have also shown a willingness to shift the focus of their competitive analysis away from local overlaps between the parties, focusing instead on a merger's effects at the national level. While in 1997 the FTC alleged that the merger of Staples and Office Depot would harm local competition, this year's suit alleges that the transaction will reduce competition across the U.S. Similarly, in *Comcast*, the DOJ focused on Comcast's "control" of access to a large share of broadband customers nationally. This approach has important implications for the parties' ability to identify remedies that are sufficient to address the agencies' concerns.

During 2015, the agencies continued to be stringent in their approach to merger remedies, increasingly requiring that the parties identify an acceptable “upfront buyer” before accepting divestiture packages. This requirement can add months to the review process, as the merging parties need to identify a buyer, negotiate a divestiture agreement, and have continued to require broad divestiture packages, which in some recent cases included assets outside the relevant market of concern. For example, the FTC conditioned clearance of the merger of Holcim and Lafarge on the divestiture of several cement plants and terminals, including a plant and a terminal in Canada, which the FTC alleged were necessary to remedy competitive concerns in northern U.S. markets.

The recent “failed” divestiture in connection with Albertsons’ acquisition of Safeway is likely to prompt even more scrutiny of proposed remedies. In January 2015, Albertsons agreed to sell 146 supermarkets to Haggen Holdings, a small regional supermarket chain, to obtain FTC’s approval to acquire Safeway. In September, a few months after it acquired the stores, Haggen filed for bankruptcy, announcing a plan to reorganize with only 37 stores. Numerous store closures will likely result in a loss of competition, frustrating the FTC’s efforts to maintain competition at the pre-merger level. Following the *Albertsons* debacle and a similar failed divestiture in connection with Hertz’s 2012 acquisition of Dollar Thrifty, merger parties should be prepared for a thorough review of divestiture buyers and protracted consent negotiations in transactions that raise concerns requiring relief.

With many industry-shaping mergers still under review, next year—the Obama Administration’s last year—is likely to continue to be a period of vigorous antitrust enforcement. As in 2015, the agencies are likely to continue to pursue new theories of competitive harm, take a tough approach to merger remedies, and subject difficult transactions to lengthy reviews. In this enforcement environment, careful analysis and planning will remain important for parties considering potential transactions. Merger partners should thoroughly evaluate the substantive antitrust issues raised by the transaction, considering both traditional and alternative theories of competitive harm, and develop an effective remedy strategy early on. Finally, risk allocation and other antitrust-related provisions in transactions agreements will continue to be critical and will need to reflect the increased risk of protracted investigations and potential litigation.