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Evolving Scrutiny in U.S. Merger Enforcement and its Impact on Dealmaking

By: Brandon S. McCoy, Jennifer T. Wisinski, Jacqueline K. Shipchandler

Antitrust regulatory risk for mergers and acquisitions in 2022 remains high: not only do proposed transactions continue to face heightened scrutiny, but the evolving enforcement standards from U.S. antitrust authorities may further increase deal uncertainty. Recent developments in antitrust cases, as well as congressional testimony and speeches by leaders from the Antitrust Division of the Department of Justice ("DOJ") and the Federal Trade Commission ("FTC") demonstrate the agencies' focus on aggressively challenging transactions that they perceive to be anticompetitive.

Potential merger parties should know that the agencies are not playing with the same playbook that has been used historically. In particular, the key changes include:

- The agencies are revising the Merger Guidelines and enhancing their toolkits for evaluating and challenging anticompetitive transactions;
- The agencies appear more willing to rely on structural presumptions of coordinated harm in highly concentrated markets;
- The agencies are pushing back on proposed structural remedies that do not adequately remedy the underlying competitive harm in transactions.

What does this mean for parties contemplating a transaction? Engaging antitrust counsel early in the transaction process is critical to evaluate the potential for challenges by the agencies and consider potential efforts to mitigate the risk. In addition, potential merger parties should take the risk into account in negotiating the merger agreement, from the covenants to closing conditions to termination rights and associated fees.

Recent Congressional Testimony from Leadership of the Agencies

In Congressional testimony on September 20, 2022, Jonathan Kanter, Assistant Attorney General for DOJ's Antitrust Division, and Lina Khan, Chair of the FTC, emphasized their commitment to "strengthen[ing] antitrust enforcement," including "pursu[ing] litigation to block anticompetitive mergers" and bringing "difficult antitrust cases." [1] Concerns regarding weakening competition have paved the way for vigorous enforcement by both agencies during an historic surge in deal-making and reportable transactions over the past two years. Khan

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[1] Prepared Remarks of Jonathan Kanter, Assistant Attorney General of the Antitrust Division, in Testimony Before the Senate Judiciary Committee Hearing on Competition Policy, Antitrust and Consumer Rights, https://www.justice.gov/opa/speech/assistant-attorney-general-jonathan-kanter-antitrust-division-testifies-senate-judiciary (Sep. 20, 2022); *see also* Prepared Statement of the Federal Trade Commission Before the United States Senate Committee on the Judiciary Subcommittee Hearing on Competition Policy, Antitrust and Consumer Rights, "*Oversight of the Enforcement of the Antitrust Laws*," at 3 (hereinafter, "Khan Statement," https://www.ftc.gov/legal-library/browse/oversight-enforcement-antitrust-laws-prepared-statement-federal-trade-commission-subcommittee (Sep. 20. 2022).

noted that the agencies are focused today not only on anticompetitive transactions involving direct competitors, but also on non-horizontal transactions and forward-looking competitive harm.[2]

Kanter and Khan also touted their recent enforcement efforts. Since Kanter's confirmation in November 2021, "the Division has challenged or obtained merger abandonments in six cases, [while several] other transactions were abandoned after the parties were informed that they would receive second requests." [3] Similarly, Khan noted that the FTC had sued to block six mergers in FY 2022 and that parties had abandoned several other transactions that were likely to be challenged by the Commission.[4] According to Kanter, "the Division will litigate more merger trials this year than in any fiscal year on record." [5]

The shift in enforcement strategy can be traced back to the start of the Biden administration, when President Biden pledged that antitrust enforcement would be a cornerstone of protecting the "American promise of a broad and sustained prosperity" noting that:

> *Robust competition is critical to preserving America's role as the world's leading economy. Yet over the last several decades, as industries have consolidated, competition has weakened in too many markets, denying Americans the benefits of an open economy and widening racial, income, and wealth inequality*.[6]

The agencies' aggressive approach has not always been successful, however – in recent weeks, DOJ suffered two high profile losses in antitrust merger challenges of UnitedHealth Group's acquisition of Change Healthcare and US Sugar Corp.'s proposed acquisition of Imperial Sugar. DOJ is reviewing its options in these cases, but continues its commitment to bringing hard cases, sending a message to companies that they should continue to expect enhanced scrutiny of transactions and be prepared to litigate in close cases.

Against this backdrop are several important takeaways for proposed merger parties:

1. Efforts to Strengthen Merger Enforcement Tools

The federal antitrust authorities are actively working to strengthen and enhance their tools for evaluating and challenging potentially anticompetitive transactions. In January 2022, the agencies began the process of revising the Merger Guidelines that provide the analytical framework and enforcement policies employed during the merger review process. Concerned that the existing approach "has led to underenforcement and markets

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[2] Khan Statement at 5.

[3] Kanter Remarks.

[4] Khan Statement at 3.

[5] Kanter Remarks.

[6] Executive Order on Promoting Competition in the American Economy, Exec. Order No 14, 306, 86 Fed. Reg. 36,987, https://www.whitehouse.gov/briefing-room/presidential-actions/2021/07/09/executive-order-on-promoting-competition-in-the-american-economy/ (Jul. 14, 2021).

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that are more concentrated and less dynamic,"[7] the stated goal of the planned revisions is to better reflect modern commercial realities and to better detect and prevent anticompetitive transactions.

The agencies are also reviewing the information that parties currently submit in connection with Hart-Scott-Rodino ("HSR") filings to assess what "additional information we need to most effectively and efficiently identify transactions that warrant a deeper investigation."[8] As part of this review, the FTC's Khan indicated that they will likely initiate a rulemaking process to require merging parties to submit upfront probative information about their proposed transactions.

The agencies also continue to strengthen their partnerships with other interested governmental stakeholders – state Attorneys General, as well as other federal agencies whose operations touch on competitive issues – to ensure a holistic approach toward promoting and protecting competition.

In addition, both Kanter and Khan asked Congress for additional funding, noting that they "lack the resources to fully address [the] challenges" they are facing.[9] Khan described the FTC as "outgunned one to 10" in litigation, and Kanter noted that the Division has 350 fewer employees than it did it 1979.[10] The requested funding may be partially addressed by the Merger Fee Modernization Act, which passed the U.S. House of Representatives on September 29th by a vote of 242-184. [11] The bill will raise HSR filing fees to $2.25 million for large transactions valued at $5 billion or more, while also lowering the filing fees for small- and medium-sized transactions. The bill, which will need to pass the Senate before becoming law, is supported by the Biden Administration as a way of providing additional resources for those transactions that often require the most extensive review and making the filing fee regime fairer and better targeted.[12]

2. Analytical Focus on Market Realities and Structural Presumptions

The ongoing review of the Merger Guidelines highlights the agency leadership's concerns that merger enforcement has been insufficient to protect U.S. competition in recent years. In a speech at the Georgetown Antitrust Law Symposium earlier this month, Kanter observed that merger enforcement has become

[7] Khan Statement at 7.

[8] *Id.* at 8.

[9] Anna Edgerton & Leah Nylen, *Biden's Antitrust Chiefs Seek Funds for Strong Enforcement*, THE WASHINGTON POST, https://www.washingtonpost.com/business/on-small-business/bidens-antitrust-chiefs-seek-funds-for-ambitious-enforcement/2022/09/20/4ac12d8a-393c-11ed-b8af-0a04e5dc3db6_story.html (Sep. 22, 2022).

[10] *Id.*

[11] H.R. 3843, Merger Filing Fee Modernization Act of 2022, https://rules.house.gov/sites/democrats.rules.house.gov/files/BILLS-117HR3843RH-RCP117-66.pdf

[12] https://www.whitehouse.gov/wp-content/uploads/2022/09/H.R.-3843-SAP.pdf

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"disconnected from the competitive realities of our economy."[13] Kanter expressed frustration with the existing approach, characterizing current merger-enforcement as a "sometimes-artificial exercise" and stating that "[w]e focus too much on a small handful of models predicting price effects, and lose sight of the competition actually at stake."[14]

Kanter stated that the existing approach used when enforcing Section 7 of the Clayton Act "leaves underenforced a statute that was meant to be prophylactic" in preventing anticompetitive transactions. He emphasized that the Supreme Court has said that Section 7 creates a relatively expansive definition of antitrust liability and that to show that a merger is unlawful, a plaintiff need only prove that its effect *may be* (not *will* be) substantially to lessen competition.[15] Kanter highlighted the anticompetitive risk of oligopoly behavior (which can result in concerted behavior that does not require either tacit or explicit agreement), and that the courts "have long explained that on the basis of an increase in concentration in a highly concentrated market, the Agencies and the courts should presume a merger creates this risk."[16]

Particularly noteworthy is Kanter's statement dismissing those in antitrust policy circles who "suggest that plaintiffs should need more than a structural presumption to demonstrate a risk of harm from coordinated effects. Under this view, the plaintiffs bear the burden of *also* demonstrating that the market has some special vulnerability to coordination."[17] According to Kanter, placing the burden on plaintiffs to demonstrate the risk of coordination contradicts the long line of cases applying the structural presumption.

In a case filed shortly before Kanter's speech, DOJ appeared to base its challenge on the presence of structural presumptions of harm based on industry concentration, rather than a market-based analysis of post-transaction coordinated effects. On September 15, 2022, DOJ filed suit to block ASSA ABLOY AB's acquisition of a division of Spectrum Brand Holdings, Inc., its largest competitor in the residential door hardware industry.[18] The Complaint alleges that the proposed transaction is presumptively unlawful based on market concentration levels. It contains a detailed description of the market concentration and head-to-head competition between the parties. It alleges that the proposed transaction would also increase the likelihood of coordination in highly concentrated markets, but it does not include specific allegations of potential coordinated effects in those markets. The *ASSA ABLOY* Complaint, along with Kanter's speech, indicates that DOJ and the FTC are likely intending to shift from the prevailing practice of identifying industry-specific potential coordinated effects toward

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[13] Prepared Remarks of Jonathan Kanter, "*Respecting the Antitrust Laws and Reflecting Market Realities,*" Georgetown Antitrust Law Symposium, https://www.justice.gov/opa/speech/assistant-attorney-general-jonathan-kanter-delivers-keynote-speech-georgetown-antitrust (Sep. 13, 2022).

[14] *Id.*

[15] *Id.*

[16] *Id.*

[17] *Id.*

[18] Complaint, *United States v. ASSA ABLOY AB and Spectrum Brands Holdings, Inc.*, 1:22-cv-012791, https://www.justice.gov/opa/press-release/file/1535131/download (Sep. 15, 2022).

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utilizing a presumption of competitive effects more often as the Merger Guidelines review continues. Whether the courts will be receptive to this approach remains to be seen.

3. Challenges to Proposed Structural Remedies

The *ASSA ABLOY* case also highlights the agencies' reluctance to accept proposed structural remedies that are insufficient to preserve existing competition. The parties proposed selling of parts of ASSA ABLOY's business that sell residential door hardware in the United States as a way of resolving anticompetitive concerns from the transaction. The Complaint dismisses the proposed remedy as wholly insufficient to preserve competition:

> *The touchstone of any appropriate antitrust remedy is the immediate, durable, and complete preservation of competition. Merely transplanting assets from one firm to another is not an effective antitrust remedy because it creates unacceptable risks of diluting the intensity of competition—the risk of creating a firm with less incentive, ability, or resources than the original owner to use the divested assets in service of competition, the risk of entanglement or conflict between the buyer and seller of the divested assets, and the risk of the buyer liquidating or redeploying the divested assets. Defendants bear the heavy burden of establishing that any remedy they propose meets these exacting standards, especially given the substantial competitive problems their proposed deal presents, and they cannot meet that burden here.*
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> *Defendants have not disclosed all of the details of their proposed "remedy" and have not identified any potential buyer for divested assets, but they have disclosed some information about the assets they propose to divest to try to "fix" their flawed transaction. In particular, the parties offered to divest portions of ASSA ABLOY's Mechanical Residential business unit relating only to the EMTEK brand and portions of ASSA ABLOY's Global Smart Residential business unit relating only to Yale and August smart locks sold in the United States and Canada. These partial divestitures would be insufficient to preserve the intensity of existing competition. They would split up existing business units, cutting off the divested assets from the organization, resources, and efficiencies that have allowed ASSA ABLOY to be a leading competitor in the United States premium mechanical door hardware and smart lock markets.*
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> *The parties' proposed divestitures would be insufficient even if a transfer of assets were executed flawlessly, but the complex carving out (and in some cases splitting) of manufacturing capacity, warehouses, personnel, intellectual property, supply chain relationships, and other resources is virtually guaranteed to be anything but flawless. American consumers should not be forced to underwrite this risky experiment in corporate reorganization.*[19]

ASSA ABLOY is not the first recent case in which DOJ has scrutinized and rejected a proposed structural remedy – Kanter noted in his Georgetown speech that competing container handling equipment companies abandoned their transaction after DOJ informed them that their proposed settlement – selling off the "least desirable assets to placate the department" – was inadequate to resolve DOJ's competitive concerns with the

[19] *ASSA ABLOY* Complaint at ¶¶ 83-85.

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transaction. Khan similarly noted that the Federal Trade Commission “strongly disfavor[s] structural remedies and will not hesitate to reject proposed divestitures that cannot fully cure the underlying harm.”[20]

ASSA ABLOY also illustrates that discussions between parties regarding antitrust concerns, regulatory risks, and remedies can be used as evidence against the proposed transaction. The Complaint notes that ASSA ABLOY executives were “having daily calls on antitrust” and the parties had disagreements about how to handle the potential regulatory risks of the transaction. Whether DOJ is correct in its claim that, by proposing a divesture remedy, the parties “effectively conceded that their proposed transaction would harm competition” is an open question. Nevertheless, the case illustrates the importance of having antitrust counsel involved in deal negotiations from an early stage – not just to assess the potential anticompetitive harm/procompetitive benefits of the transaction, but to advise on regulatory risks and litigation strategy while deal counsel is managing the due diligence and transaction negotiations.

Final Thoughts and Takeaways

What is clear today is that potential merger parties should be prepared for the unexpected in terms of antitrust enforcement. Under the current administration, the federal agencies are actively bringing hard cases – even in the face of judicial losses – and are evaluating ways to revise their framework for assessing anticompetitive harm to better capture what they perceive as the modern realities of competition.

As a result, it is more important than ever for companies exploring transactions in consolidated industries to work with experienced counsel to develop a plan early on to evaluate and address potential antitrust concerns and their potential impact on the ability to complete the transaction, as well as the associated timing and cost. Antitrust counsel can evaluate the potential for challenge as well as work to identify information regarding verifiable efficiencies and other countervailing factors that can be used to offset claims that the proposed transaction will have anticompetitive effects. Discussions of potential divestitures/antitrust remedies should be handled as part of a comprehensive legal strategy that incorporates antitrust/litigation risks as part of the overall deal negotiation and due diligence process. Corporate counsel can advise on merger agreement terms aimed at allocating antitrust risk between the parties, including who is responsible for working to resolve any challenges and what actions may or may not required by such parties as well as conditions to closing, an appropriate “outside date” and termination rights and fees.

[20] *See* Khan Testimony at 6.

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