Merger Remedies:
General Principles and Approaches

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Goal of Merger Remedies

The goal of remedies in a merger case is to preserve or restore competition and to prevent or correct the exercise of market power that may result from a merger or acquisition. In doing so, such remedies enable a modified outcome to such transactions while allowing for the realization of merger benefits.[1] This goal is achieved by beginning with a thorough examination of the details of each case and of the prospective harm or competitive detriments that result from the action. After such consideration, remedies may be crafted to address the identified harm. The resulting goals may include maintaining or restoring pre-merger competitive conditions, creating a competitor to replace the acquired firm, encouraging or enabling entry by a new firm, or enabling expansion by a small existing competitor. The remedy or remedies should address the competitive harm from the merger and should fit the facts of the case and characteristics of the relevant market. There should be a close and logical nexus between the theory of harm and the remedy. While a number of approaches have proven successful in many cases, there is no rigid set solution in approaching merger cases. The effective relief should address the hard and, where feasible, preserve the efficiencies the merger aimed to accomplish.

Process for Obtaining Merger Remedies

Court- or Agency- ordered Remedies

There are two processes for obtaining merger remedies. There are court- or agency-ordered remedies in which a decision is issued after a hearing or other proceeding. These decisions either stop a merger or order a specific remedy. Court-ordered remedies coincide with a judicial system where a court possesses the authority to hear such cases and to impose remedies. Examples of nations with such judicial systems include the United States, Canada, and Chile. Alternatively, agency-ordered remedies coincide with an

[1] ICN Merger Working Group: Analytical Framework Subgroup, Merger remedies review project, Report for the fourth ICN annual conferences, Bonn – June 2005, p. 1.

administrative system, such as the one found in the European Union, where an institution has the authority to review the merger and to block the transaction or to approve negotiated settlements in which parties to the transaction undertake agreed-to remedies. Some nations, including the U.S., implement both judicial and administrative processes in issuing merger remedies.

In the United States, the Federal Trade Commission (FTC) and the Department of Justice (DOJ), each have authority to challenge anticompetitive mergers. These agencies have their own processes for obtaining court or agency ordered remedies and both serve as strong examples of good practices in obtaining merger remedies.

The FTC and DOJ processes involve the seeking of preliminary or permanent injunctive relief for violations in U.S. District Court. A substantive trial on the merits and the development of an evidentiary record follow. The FTC alternatively may seek permanent relief in agency administrative proceedings.

Negotiated Settlements

The second process for obtaining a merger remedy is through negotiated settlements. These settlements avoid the need to prohibit the merger and can allow any merger-specific efficiencies to be realized. Such efficiencies may include, but are not limited to, production expansion or efficiency, cost reduction, new or improved product development and increased investment in innovation.[2]

Negotiated settlements avoid the expenditure of time and resources to prepare and litigate the case, yet they provide for final and enforceable orders. Countries including the United States, the European Commission, Chile, and Brazil have practices in place for achieving negotiated settlements.

[2] ICN Recommended Practices for Merger Analysis at p. 1.

In the United States, the FTC settlement process involves a binding agreement entered with merging parties. In the agreement, the parties waive their right to make the FTC prove its case, and the FTC usually allows the merger to proceed. Every settlement agreement contains a provision waiving further procedural steps and the right to appeal or challenge the final consent order. The Commission also issues a complaint, alleging how the proposed merger or acquisition would violate the law. Once the Commission accepts the consent agreement, the proposed consent order, the complaint, and the consent agreement are placed on public record. For the next thirty days, interested parties may submit comments on the proposed order. The comments received will become part of the public record. The Commission will also place on the public record an explanation of the complaint and of the order's provisions and the relief to be obtained along with any other information the Commission believes may help interested parties. Once this thirty-day period concludes, the Commission may vote to make the order final, or it may reject the settlement and take further appropriate action. This may include negotiating further relief, challenging the merger altogether, or closing its investigation without action. In the vast majority of cases, the Commission makes the order final as first negotiated, or makes clarifying modifications.

The DOJ follows a very similar substantive process, but does so in a court setting. It negotiates appropriate relief, and then files its complaint and proposed remedy in a federal court. DOJ also releases an explanatory statement and the court will wait for 60 days in case third parties wish to submit their views. At the end of that process, the court will issue the final decree.

In Chile, Fiscalía Nacional Económica ("FNE") is the primary body responsible for merger review and analysis. The review begins when parties to the transaction communicate their intention to merge to the FNE prior to consummating the merger.[3] The FNE will undergo a thorough investigation and analysis of the proposed transaction often soliciting information from the parties to the transaction. After such review, the FNE will conclude the process in one of three ways, including: (1) the issuance of a decision to take no further action; (2)

[3] FNC, Guide for the Analysis of Merger Transactions, p. 2.

reaching an out of court settlement with the parties that then will be formally approved by the Tribunal de Defensa de la Libre Competencia ("TDLC"); or (3) presenting an inquiry about the transaction to the TDLC.[4] In the event that the FNE decides to attempt to reach an out of court agreement among the parties and the parties are interested in such an agreement, the grounds for the agreement will be established and a time schedule for negotiations will be set.[5]

In Brazil, the Conselho Administrativo de Defesa Econômica ("CADE") and its constituent branches oversee the merger review process, which primarily begins with the parties to a transaction notifying the competition authority of their intended transaction. The parties are able to negotiate remedies with CADE from the time they notify the authority until thirty days after the case has been sent to the Tribunal for review.[6] The negotiations are intended to modify the original transaction so as to preserve the transactions intended efficiencies while eliminating some of the harmful, anticompetitive effects the transaction produces. Ultimately, the Tribunal must approve the settlement.[7]

Types of Remedies

There are two main types of remedies: (1) structural remedies and (2) conduct, or behavioral, remedies.

Structural remedies, such as divestitures, are the preferred basic relief for horizontal mergers. The goal is to maintain, restore, or increase the number of independent competitors. These types of remedies rely on market forces to maintain or restore competition following successful divestiture. Conduct, or behavioral, remedies prohibit certain conduct and require certain affirmative actions. They usually constrain and/or regulate the merged firm's business conduct, and they generally require monitoring by

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[4] *Id.*
[5] *Id.*
[6] http://www.jonesday.com/files/Publication/ee7ed7df-d4fd-4ff4-bf76-55a933c7cf49/Presentation/PublicationAttachment/f4ef687d-1c40-4ffc-a1e9-5ae02b69463f/ABA%20Antitrust%20Source%20Article%20-%20A%20Fundamental%20Shift.pdf
[7] *Id.*

competition authorities. Behavioral-only remedies are generally disfavored as such remedies are highly regulatory and do not necessarily effectively counter the anticompetitive effects of a transaction. Unlike structural remedies, behavioral remedies require constant monitoring, they are difficult to control, they may be competitively harmful, and they are less responsive to market dynamics.

However, certain conduct remedies can serve to complement structural remedies, and full and effective relief may require the use of both structural and conduct remedies. For example, at the 2011 OECD Policy Roundtable on Remedies in Merger Cases, the delegation from Chile explained that its competition authority implements two types of remedies. The first are divestitures, and the second are "forward-thinking" remedies.[8] These "forward-thinking" remedies either complement a divestiture or seek to counter the competitive effects of the transaction. The delegation used the example of a 2004 TV cable merger in which the Competition Tribunal ordered the complete divestiture of assets in certain markets and, in addition, prohibited the resulting merged entity from participating in such markets in the future.[9] Further examples of "forward-thinking" remedies include the requirement that part of the business remains in a publically traded corporation and subject to securities rules, and the requirement that the merged entity notify the authorities of its involvement in any further mergers or acquisitions.[10]

Structural Remedies

The first step in contemplating structural remedies is the examination and identification of the harm that results from the merger or acquisition. This harm is often the development or an increase in the merging firms' market power that results from the loss of competition.

The remedies applied will directly address the changes to the market structure caused by the merger or acquisition. Some examples of structural remedies include: 1) the transfer of market position or share from the merging firms to another firm; 2) the creation of a new

[8] OECD 2011 Roundtable, Summary of Discussion p. 292.
[9] *Id.*
[10] *Id.* Note: Notification is voluntary in Chile.

competitor or strengthening of a smaller existing competitor; 3) the elimination of entry or expansion barriers and/or the encouragement of new entry; and 4) the elimination of the harm created by ownership, control, or access. The implementation of structural remedies is more certain and requires the administration of fewer resources as competitive market dynamics lead future performance.

The most common structural relief is divestiture, which is the sale of a business or certain assets to create a competitor that will replace the competition lost in the merger. A divestiture usually requires the sale of stock assets, or a business. Another form of structural relief is a licensing agreement, which requires a firm to license its rights to others in the market to use property originally held exclusively by the firm. Both divestitures and licensing agreements target buyer-participants within the market and aim at either creating or bolstering the market participant's ability to compete in the new market landscape.

Divestitures

Divestitures are the most common form of structural relief. The initial issue when implementing this form of relief is deciding what and how much should be divested. The form and scope of the divestiture should flow from the facts of the case. This takes into consideration how the firms conduct their business and the nature of the market in which the firms operate. The examination does not solely look at the product market overlaps between the firms; instead, the examination considers each firm as a whole.

What should be divested depends on the form of the transaction and the source of the harmful effects. Some of the assets that are commonly divested include stock, share capital, voting securities, tangible assets such as business units, and intangible assets such as intellectual property. How much should be divested depends on the theory of harm and on what is required for full and viable relief. Complete divestiture, for example, would restore the pre-merger firm. Partial divestiture would require divesting less than a stand-alone business entity.

Often, the proposed "divestiture" comes in the form of a divestiture package with various types and quantities of assets included for divestiture. These packages can be input packages, retailing packages, and services packages comprised of such assets as autonomous subsidiaries, machinery, and know-how of the industry.[11]

The FTC published a study in 1999 on the Commission's divestiture process and discussed what forms of divestitures tend to be the most successful.[12] The study stressed the importance of considering the motives behind various divestiture packages. For example, the study found that although most divestitures create a viable competitor within the market, some of the merging entities required to divest assets may seek out marginally acceptable buyers and may use alternative methods to impede the buyer's success in the given market. A common form of a divestiture that reflects strategy is the divesting of machinery and operation facilities to a buyer without providing the buyer with the "know-how" of the operation processes so that the buyer may be able to effectively use these assets to compete in the market. The study also discusses potential obstacles to effective divestitures as well as the ways these obstacles can be overcome. [13]

Licensing/ Intellectual Property Rights

Licensing agreements require the licensing of rights to use or access property, technology, or infrastructure originally held by someone else. Licensing can often enable entry by providing a new firm with rights or access and the ability to compete. For example, a license of intellectual property prominently used in a market to a new competitor can allow that new competitor to enter the market.[14] This ultimately enables expansion by

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[11] http://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&ved=0CCgQFjAA&url=http%3A%2F%2Fwww.ftc.gov%2Fsites%2Fdefault%2Ffiles%2Fattachments%2Fmerger-review%2Fdivestiture.pdf&ei=TgWGU_32OdW_sQTa0ILwDQ&usg=AFQjCNFLYU2yr8IiQUl1x0tZifIVSA7Bjg&bvm=bv.67720277,d.cWc&cad=rja.

[12] *Id.*

[13] *Id.*

[14] In *Shell/BASF*, the parties agreed to grant a non-exclusive, non-transferrable license on certain catalysts to any interested third party, allowing for third parties to continue to compete or to enter the market (ICN Merger Working Group: Analytical Framework Subgroup, Merger remedies review project, Report for the fourth ICN annual conferences, Bonn – June 2005, Appendix D). ; *In the Matter of Chicago Bridge * Iron Company N.V. et al*., Chicago Bride and Iron was ordered to license to the acquirer all rights to use

eliminating entry barriers in an existing license. It often terminates exclusive rights and requires modification to the scope of use and or/geographical restrictions.

Exclusive licenses are generally preferred. These types of licenses prohibit the grantor of the license from licensing any of the same rights to any other entity for the duration that the original grantee holds the license. This type of licensing agreement is preferred because it maximizes the licensee's incentives to invest in divested businesses and innovate. Non-exclusive licenses, however, may be appropriate to preserve efficiencies and to allow a merged firm to continue to compete in retained businesses. The form of license offered may depend of pre-existing ownership or license rights.

Continuing entanglements can be a concern. Perpetual, fully paid-up and royalty-free licenses with other "ownership-like" rights are generally easier to administer. Another concern is third parties who may have rights. This concern is addressed usually by having the merging firms obtain consents and approvals from such third parties.

Other Considerations

In addition to considering which types of remedies provide the best relief for the offset in competition, it is important to consider factors such as timing and risk in implementing the proposed remedies. Some remedies, such as licensure, are only effective if implemented within a certain and immediate timeframe. Therefore, it is often beneficial to begin considering possible remedies early in the merger evaluation process. In addition, every remedy poses some element of risk as all remedies rely on future predictions within the affected market. The most effective and stable remedies are the ones that are implemented and structured to accommodate both present and future market impact.

Behavioral Remedies

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commingled intellectual property of the merged firm on a perpetual, non-exclusive, sublicenseable, royalty-free basis.

Behavioral-only remedies are generally disfavored as relief for unlawful horizontal mergers. Such remedies are highly regulatory. They require constant monitoring,[15] they are difficult to control, they may be competitively harmful, and they are less responsive to market dynamics.[16] In addition, such remedies are more difficult to draft, more costly to administer, and easier than structural relief to circumvent. Effectiveness, enforceability and continuing entanglements are a concern. Despite all of these negative implications, conduct remedies may be appropriate in certain--rare–circumstances, where a divestiture would be disproportionately overbroad or infeasible and where significant efficiencies may be lost if the merger is prohibited.[17]

While conduct remedies are disfavored as the sole source of relief for horizontal mergers, such remedies are often used to support structural relief.[18] For example, transitional supply provisions may be incorporated to supply a product for a short period following the merger. There may be technical assistance provided at an acquirer's request. Employee provisions may also be made. Such provisions would provide incentives for the seller's employees to seek employment with the acquirer by, for example, prohibiting the enforcement of non-compete clauses.

In the *Braskem/Quattor* case, the Brazil competition authority sought to resolve the anticompetitive harm by implementing behavioral remedies. Although the transaction led to a monopoly within the market, the behavioral remedies were considered to be more appropriate given the adverse effects structural remedies would have had on other market participants.[19] In addition, the behavioral remedies enabled the authority to exercise oversight over the merged entity and provided tools to prosecute abuses by the new entity

[15] *See, Drager/Air-Shields*.
[16] *See, Mediswitch/QEDI*.
[17] E.g. In *Valio/Aito Maito,* prohibiting the deal would likely result in an even greater decrease in milk supply and deliveries for other cooperatives in the market (ICN Merger Working Group: Analytical Framework Subgroup, Merger remedies review project, Report for the fourth ICN annual conferences, Bonn – June 2005, Appendix F).
[18] *See, GE/InVision*, *Shell/DEA and BP/VEBA*, *Drager/Air-Shields* and *Nuon/Reliant Energy*
[19] OECD 2011 Roundtable, Summary of Discussion p. 294.

more easily.[20] The Brazil competition authority was equipped with tools to counter the competitive harm that followed the merger.[21]

Remedies for Non-Horizontal Mergers

The discussion of remedies thus far has been in the context of horizontal mergers; however, there are other forms of mergers, including vertical mergers and conglomerate mergers, that may require a different approach to relief. Vertical mergers are mergers that combine firms at different levels of the supply or distribution chain, having a customer- supplier relationship.[22] For example, a merger between a food distribution warehouse operator and a retail supermarket chain would be a vertical merger with the food distribution warehouse being the supplier and the retail supermarket chain being the customer. Conglomerate mergers take place when the combining firms are neither direct competitors nor have a customer-supplier relationship. The firms may be in related markets or firms that produce complementary products. For example, a merger between a manufacturer of toothpaste and a manufacturer of battery-powered toothbrushes would be a conglomerate merger as the two entities are neither competitors nor do they have a customer-supplier relationship.

Non-horizontal mergers are usually pro-competitive and have substantial efficiency benefits that result from integrating related activities. Such benefits may include lower transaction costs, synergies that improve design, production and distribution of products, and the elimination of double markups. As a result, these mergers are less likely to create competitive concerns than horizontal mergers. Despite the benefits and efficiencies associated with non-horizontal mergers, there could be some potentially harmful effects. A non-horizontal merger might create or increase a merged firm's market power and/or enhance the ability or incentives to exercise such power to the detriment of consumers or competition. This creates foreclosure concerns, concerns about access to the market, and information sharing concerns.

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[20] *Id.*
[21] *Id.*
[22] The customer- supplier relationship is often referred to in terms of downstream and upstream, with the customer considered to be "downstream" and the supplier considered "upstream."

Structural remedies are often overbroad, inappropriate, or not feasible for providing relief to the harm that results from non-horizontal mergers. Substantial efficiencies may be lost if the merger is prohibited or if divestiture is ordered. Conduct remedies may be appropriate relief for the concerns that flow from vertical mergers. Continued oversight may be needed, but this may be an unavoidable trade-off to minimize the loss of efficiencies.

Conclusion

The "problem solving" approach is the most effective method to employ in designing merger remedies. The analysis begins with an examination of the harm or harms that result from the merger or acquisition. This harm to competition from the merger is "the problem." Then, the merger related factors or situation that create or cause the problem are identified. A remedy or set of remedies are chosen to fix the problem(s) as completely and effectively as possible. Finally, the solution or set of remedies is evaluated so as to preserve the efficiencies that result from the merger or acquisition.