Merger Enforcement and Non-Price Effects

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Non-Price Considerations in Merger Enforcement

- Merger law is concerned with transactions that reduce competition and increase market power.
- Market power (of a seller) can be exercised through a variety of ways that reduce the net value of a transaction to the buyer: increasing the price, decreasing the quality, imposing disadvantageous non-price contractual terms.
- If antitrust law is to fully protect the competitive process, it should be concerned with the potential for non-price as well as price effects that result from reducing competition.
- But some commentators are skeptical: "[T]he concern of merger policy with oligopoly is a concern with market output and price/cost relationships, and only secondarily and implicitly with innovation. The principal concern is that a merger will create a more concentrated market structure permitting oligopolists to increase their prices further above their costs." - Areeda/Hovenkamp

Justification for Non-Price Approaches

- Economics: Firms compete across multiple dimensions, of which price is only one. Firms compete to differentiate themselves, horizontally and vertically.
- Text: Section 7 of the Clayton Act prohibits mergers where the effect in any market "may be substantially to lessen competition" – not "substantially to lessen PRICE competition."
- Case law: *Philadelphia National Bank*, in which Supreme Court established structural presumption, was concerned with competition across numerous dimensions: "price, variety of credit arrangements, convenience of location, attractiveness of physical surroundings, credit information, investment advice, service charges, personal accommodations, advertising, miscellaneous special and extra services."
- Merger Guidelines, § 1: "Enhanced market power can also be manifested in non-price terms and conditions that adversely affect customers, including reduced product quality, reduced product variety, reduced service, or diminished innovation. Such non-price effects may coexist with price effects, or can arise in their absence."

Example of Non-Price Effect – Reduction in Product Quality

- Coordinated quality effects in *H&R Block*:
  - "TaxACT has emphasized high-quality free product offerings as part of its business strategy."
  - Post-merger, "HRB and Intuit may find it 'in their mutual interest to reduce the quality of their free offerings.'"
- Unilateral quality effects in *H&R Block*:
  - "A merger is likely to have unilateral anticompetitive effect if the acquiring firm will have the incentive to raise prices or reduce quality after the acquisition."
  - "[T]he evidence discussed above indicat[ed] direct price and feature competition between HRB and TaxACT."

Example of Non-Price Effect – Lessened Innovation

- AMAT/TEL merger involved two suppliers of non-lithography semiconductor manufacturing equipment.
- There was little overlap in existing product markets; but they were "the two largest competitors with the necessary know-how, resources and ability to develop and supply high-volume non-lithography semiconductor manufacturing equipment." DOJ Press Release.
- TEL CEO expressed surprise that DOJ was concerned with "products under development, which are not sold to the customer, [where TEL] cannot have any [current] market share."
- But Section 7 of the Clayton Act reaches competition "in any line of commerce *or in any activity affecting commerce in any section of the country*" – that seems to cover innovation of new products with sales only in the future.

Example of Non-Price Effect – Exclusionary Contract Terms

- In Charter/TWC, the government's complaint alleged that "TWC has been the most aggressive MVPD in the industry in seeking and obtaining restrictive contract provisions in its agreements with programmers that limit the programmer's ability to license programming to OVDs."
- Combining Charter and TWC would have given the merged firm "nearly 60 percent more subscribers than TWC standing alone."
- The would have given it increased "bargaining leverage to insist that video programmers limit their distribution to OVDs."
- Bargaining leverage is market power, and that power would have been exercised against the programmers by the imposition of exclusionary contractual terms.

Why Non-Price Effects are Important

- Sometimes we know price effects are unlikely
  - Price terms might be set for most customers in long-term contracts (e.g., defense industry).
  - Price regulation might establish a ceiling on potential price increases (e.g., *PNB*).
  - Parties might commit not to raise prices (e.g., *H&R Block*).
  - Rather than be unconcerned about a merger, we might look to the possibility that reducing competition will cause non-price effects. In *H&R Block*, court noted "the merged firm could accomplish what amounts to a price increase" by "limit[ing] the functionality of TaxACT's products."
- Efficiencies
  - Where plaintiff predicts price increase from merger…
  - Defendant could rebut by showing cost reductions sufficient to make price increase unlikely OR, possibly, quality improvements sufficient to justify higher prices.

Tools for Detecting Non-Price Effects

- "When the Agencies investigate whether a merger may lead to a substantial lessening of non-price competition, they employ an approach analogous to that used to evaluate price competition." Merger Guidelines § 1.
- Presumption:
  - Structural presumption is agnostic about how increased market power will be exercised
  - Implicitly covers non-price as well as price effects
- Documents and testimony:
  - ABI/Modelo: Bud Light Lime, introduced to compete against Corona, was "invading aggressively and directly the Corona territory" according to a Modelo exec
  - Charter/TWC: terms in TWC's contracts that limited online distribution options for programmers
- Quantitative evidence:
  - Challenging, but possible, to model non-price effects
  - Regressions might show negative relationship between market share (or market concentration) and R&D activity

Limits of Non-Price Considerations

- Antitrust law is not a broad social welfare prescription.
- Some mergers might cause a variety of detrimental effects that reduce social welfare, but these could be unconnected to any change in the competitive dynamic:
  - Layoffs resulting in a loss of employment
  - Reduction in data privacy standards
  - Lesser environmental protections
- Non-price effects of mergers are only a consideration in antitrust law when they result from a loss of competition.