

**JOINT COMMENTS OF THE AMERICAN BAR ASSOCIATION’S
SECTION OF ANTITRUST LAW AND SECTION OF INTERNATIONAL LAW
ON
THE UNITED KINGDOM COMPETITION COMMISSION’S MAY 2008
CONSULTATION DRAFT GUIDELINES ON APPLICATION OF DIVESTITURE
REMEDIES IN MERGER INQUIRIES***

August 18, 2008

The views stated in this submission are presented jointly on behalf of these Sections only. They have not been approved by the House of Delegates or the Board of Governors of the American Bar Association and therefore may not be construed as representing the policy of the American Bar Association.

The Section of Antitrust Law and the Section of International Law of the American Bar Association (“the Sections”) appreciate the opportunity to provide comments to the UK Competition Commission (“CC”) with respect to its *Consultation Draft Guidelines on the Application of Divestiture Remedies in Merger Inquiries* (“Draft Guidelines”), published in May 2008. The Sections previously provided detailed views on the CC’s *2004 Merger Remedies Guidelines* (“2004 Guidelines”). While the *Draft Guidelines* represent an evolution and refinement of the 2004 Guidelines, many of the Sections’ comments on the 2004 Guidelines remain pertinent. These comments are limited to matters that were not covered in depth in 2004, except for a few prominent issues that the Sections wish to underscore.

These comments are informed by the Sections’ experience in dealing with U.S. and non-U.S. antitrust authorities. The Sections have had substantial experience with the various merger guidelines issued by the U.S. antitrust authorities, including merger remedies guidelines issued by the Antitrust Division of the U.S. Department of Justice (“DOJ”) and the Federal Trade Commission (“FTC”).¹ These comments are meant to

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¹ See Federal Trade Comm’n, *Negotiating Merger Remedies* (Apr. 2, 2003); U.S. Dep’t of Justice, Antitrust Division, *Antitrust Division Policy Guide to Merger Remedies* (Oct. 2004).

share with you the Sections' current views based on our experience and learning to date. In addition, the views expressed here may differ from the views of the U.S. antitrust authorities and from U.S. enforcement practice.

Introduction

The Sections commend the CC on its efforts to improve its guidelines on merger remedies, especially in light of the fact that useful guidance in this area is necessarily complex because such remedies are highly fact-specific. The Sections also applaud the CC's efforts to increase transparency and share best practices through consulting professional bodies and networks worldwide. The Sections firmly believe that it is in the best interests of competition authorities, as well as parties to transactions and their advisers, to engage in constructive dialogue about how merger control regulations and procedures should evolve. In a world in which the legal issues in cross-border transactions continue to become ever more complex, the Sections believe that transparency is an important goal in merger enforcement and that nations should seek to harmonize on best practices in merger review.² In this respect, the Sections particularly welcome the *Draft Guidelines'* consideration of the merger control policy of the European Community and the *Draft Guidelines'* reference to the important contributions of the International Competition Network.³

The Sections welcome the CC's ongoing efforts to update and consolidate its various policy guidelines on the merger review process and to draw upon the CC's recent experience, judgments of the Competition Appeal Tribunal, and the CC's and the EC's research into the outcomes of prior merger remedies.⁴

The Sections endorse Part 1 of the *Draft Guidelines'* explicit recognition of the need to tailor remedies based on the particular circumstances and the time constraints involved in a particular case. It is our experience that such flexibility is particularly important in the remedies phase of merger cases. The factual issues raised in remedies

² See Int'l Competition Network, Recommended Practices For Merger Analysis at 2 (2008) (stressing that "[c]lear, comprehensive, and transparent legal and analytical standards . . . significantly, improve the predictability of enforcement actions").

³ See Int'l Competition Network, Merger Remedies Review Project: Report for the Fourth ICN Annual Conference (2005); see also Int'l Competition Network, Recommended Practices on Remedies and Competition Agency Powers (2005).

⁴ The *Draft Guidelines'* refers to two publications: Competition Commission (UK), Understanding Past Merger Remedies: Report on Case Study Research (2007); and DG Competition (EC), Merger Remedies Study (2007).

are often unique to the industries, firms, and products at issue. What works in one transaction may not work in another transaction, even in the same industry. Accordingly, it is necessary for enforcement authorities to adopt a pragmatic approach.

The *Draft Guidelines* are notable for their recognition that remedies have the potential to impose significant transaction costs on consumers as well as on the merging parties, especially where a proposed remedy may negatively affect the ability of the merged firm to achieve efficiencies or deliver other customer benefits. This sensitivity to potential costs suggests that the CC will attempt to apply its *Guidelines* in an appropriately pragmatic fashion.

Our comments are set out below. For ease of exposition, our comments are ordered and cross-referenced to the corresponding paragraphs in the *Draft Guidelines*.

Part 1 - Introduction and Context

Paragraph 1.8 sets out the factors that the CC will consider in assessing the effectiveness of potential remedies. The Sections agree with the factors set forth in the *Draft Guidelines* that the remedy must effectively redress the substantial lessening of competition that would otherwise result from a transaction. However, we respectfully suggest that the *Draft Guidelines* may benefit from a clearer statement on the standard by which the CC will assess the effectiveness of its merger remedies. Paragraph 1.8 states that effectiveness is best accomplished, where feasible, by “[r]estoring this process of rivalry through remedies that re-establish the structure of the market.”⁵ We suggest that goal should be the restoration of rivalry (the level of competition), rather than restoration of market structure. This approach is consistent with the UK Merger Guidelines, which do not presume that significant increases in concentration necessarily result in a substantial lessening of competition. The Sections suggest that a more practical and realistic standard would require the parties to restore generally the level of premerger competition. In any event, it would be helpful were the CC to enunciate its standard more clearly.

⁵ See also Paragraph 2.6 which states that “A successful divestiture will effectively address at source the loss of rivalry resulting from the merger by changing or restoring the structure of the market.”

In paragraph 1.12, the *Draft Guidelines* adopt as a core principle the concept of proportionality, a basic principle of EU administrative law. The adoption of this concept as a guiding principle suggests that the CC will exercise its prosecutorial discretion to ensure that the remedies it seeks in any case will not be disproportionate to the substantial lessening of competition that would otherwise result from a transaction. This policy statement by the CC is valuable. The Sections suggest that further guidance could be beneficial to illustrate the effect of the application of this principle on the type of remedy likely to be sought in a particular case. For example, assume a case in which the transaction would result in a substantial lessening of competition in one product line manufactured in a multiproduct plant. Assume further that the problematic product line accounts for only 10% of the plant's output, and that the only available remedy is the divestiture of the entire multiproduct plant. Under the *Draft Guidelines* would such a scenario be an "exceptional circumstance" in which the CC would not seek divestiture of the plant, or would it accept behavioral or other non-structural remedies, such as a long-term supply agreement under the proportionality principle?

Paragraphs 1.14 to 1.20 of the *Draft Guidelines* discuss the manner in which the CC will take into account the effects of proposed remedies on the customer benefits of a transaction. The Sections welcome the CC's position that it will seek to ensure that the remedies it requires will not unnecessarily impact the relevant consumer benefits flowing from a merger.

Part 2: Choice of Remedies

In discussing full or partial prohibition of a merger, the *Draft Guidelines* indicate that in some cases remediating substantial lessening of competition may require a party to reduce its shareholding in another party to below a specified level. The *Draft Guidelines* provide no indication of how an appropriate "specified minimum level" would be determined and what general factors will be considered. In order to provide more guidance on this issue, the CC may wish to consider whether it could adopt a numerical safe harbor or employ other remedies beyond divestiture of shareholdings, such as holding a purely passive economic interest without voting rights, or restricting the flow of competitively sensitive information between the parties.

Paragraphs 2.14 to 2.21 of the *Draft Guidelines* provide important and welcome policy flexibility. They indicate that although the CC generally will prefer structural remedies, it will also consider nonstructural remedies in appropriate cases. The *Draft Guidelines* note that the CC will exercise its discretion to consider such remedies where the harm to competition is expected to be very limited, or where structural remedies would be disproportionate or would negatively impact the realization of any customer benefits. The Sections commend the *Draft Guidelines* for making it clear that the CC understands that the risks and costs associated with nonstructural remedies can be significant.

The Sections welcome the CC's comity-oriented statements in paragraphs 2.23 and 2.24 of the *Draft Guidelines* that it will typically seek to consult with other interested competition authorities and in selecting remedies will appropriately take into account the remedies of other jurisdictions that may have a more substantial interest in regulating the transaction at issue. As noted above, the Sections regard international harmonization of merger reviews by all jurisdictions as important for providing consistency in remedial obligations, and welcome the CC's position on this issue. The Sections suggest that more guidance be provided on how such international cooperation would work in practice, including whether the CC may, in appropriate circumstances determine that no remedies are needed because remedies imposed in foreign jurisdictions are sufficient to remedy any competition concerns in the United Kingdom, or, to the extent such an approach may be possible under applicable statutory review timetables, wait for remedies to be decided in a foreign jurisdiction with which the transaction has a greater nexus before determining what additional remedy may be necessary to address competition concerns in the United Kingdom.

Part 3 – Divestiture and intellectual property remedies

Paragraph 3.6 of the *Draft Guidelines* provides that “the CC will take, as its starting point, divestiture of all or part of the *acquired* business.” (emphasis added) on the basis that this represents the most straightforward remedy to return competition to the status quo ante. The *Draft Guidelines* also appear to assume that divestiture of the acquired business would involve lower risk than divestiture of the acquiring party's business. The Sections respectfully question the validity of this approach as a general rule. In some cases, the antitrust authority may have developed such a substantial

amount of relevant information about both parties to enable the authority to decide which divestiture is appropriate with a relatively higher degree of confidence. This may be the case, for example, in some instances where separable, stand-alone businesses are involved, and competition would be restored equally well regardless of whether it is the acquiring party's or the acquired party's overlapping business that is divested.⁶ As noted above, the Sections suggest that the focus should be on identifying only those businesses or assets that are necessary for the restoration of effective competition to the status quo ante, rather than a focus on replicating the exact position of either the acquiring or acquired business premerger. Of course, this is not to suggest that the goal of any remedies policy should be to require divestiture of only a narrow set of core overlap assets. A particular divestiture package may need to include certain non-overlap assets if necessary to create an entity that has all that it needs to operate as a viable and effective competitor.

A presumption that the acquired party's assets should be divested suggests that an acquirer may face unnecessary difficulties in at least two types of transactions. First, where the acquirer is seeking to acquire the target in an unsolicited tender offer, a presumption that the target's business must be divested is problematic because the acquirer in a contested transaction may not have access to sufficiently detailed information concerning the target's business. Second, such a presumption suggests that an acquiring party may not be permitted to engage in a "trade up" transaction by swapping its lower quality assets for the acquired party's business. When such "trading up" transactions have had a neutral impact on competition, they have generally been permitted by the U.S. enforcement authorities.⁷ Such a presumption against trading up would impose particularly perverse outcomes in mergers where the parties overlap in only a few product lines, but where the overlap is highly asymmetrical in terms of the relative size of the businesses. Again, the standard should

⁶ In a number of cases in the U.S., the consent decrees allow the merging parties to choose either side's assets for divestiture. *See e.g.*, *United States v. SBC Commc'ns.*, 339 F. Supp. 2d 116 (D.D.C. 2004) (requiring divestiture of either party's overlapping business in the local wireless markets of concern); *United States v. Manitowoc Co.*, 2003-1 Trade Cas. (CCH) ¶73,955 (D.D.C. 2002) (requiring divestiture of either side's boom truck business).

⁷ *See e.g.*, *United States v. Monsanto Co. and Delta and Pine Land Co.*, Case: 1:07-cv-00992 (D.D.C. filed May 31, 2007), <http://www.usdoj.gov/atr/cases/f223600/223679.htm> (permitting Monsanto to acquire Delta and Pine Land, but requiring Monsanto to divest its overlapping Stoneville cotton seed business).

be whether the competitiveness of the divested entity is sufficient to maintain the level of competition in the affected market(s).

In Paragraph 3.8, the *Draft Guidelines* adopt a sunset period of 15 years with respect to prohibitions on the repurchase of any of the divested assets. Although the Sections believe that it is important to adopt clear sunset periods on such prohibitions, the Sections suggest that the CC consider adopting a system that provides for periodic review of such prohibitions to determine if the remedy is still justified. On the other hand, the temporary nature of conduct remedies requires an enforcement agency to enunciate, at least for itself, why a temporary remedy is sufficient to allow a presumably permanent combination.

Paragraphs 3.9 and 3.10 of the *Draft Guidelines* note that the CC will generally prefer the “divestiture of an existing business that can compete effectively on a stand-alone basis” rather than a package of assets that must be carved out of an existing business, but the CC will take a flexible and pragmatic approach. The Sections believe that flexibility in this respect is essential to avoid remedies that are too costly or that are disproportionate to the potential substantial lessening of competition arising from the transaction. The Sections also observe that such a pragmatic approach is consistent with the more recent practice of the U.S. enforcement authorities. In recent years, the U.S. enforcement authorities appear to have become more flexible with respect to divestitures of assets rather than the divestiture of stand-alone businesses, particularly where appropriate buyers exist that would not require a stand alone business in order to restore competition. Indeed, the U.S. authorities recognize that there is almost always a tradeoff between the quality of the assets and the quality of the buyer: where a number of high quality buyers exist, frequently the divestiture package can be more limited. Conversely, where there appear to be few viable buyers, the asset package must often be broader.

The Sections believe that, though it is impossible to address all possible circumstances, the *Draft Guidelines* would benefit from providing some illustrative, non-exhaustive, examples of where the presumption of “stand alone” businesses might not apply. For example, the presumption may not apply in industries in which assets are

regularly carved out and sold to create new businesses in ordinary course transactions.⁸ The presumption may also impose costs in an unsolicited takeover situation where a “fix-it-first” solution may be necessary to resolve shareholder concerns regarding regulatory risk. As noted above, in a contested takeover, the acquiror frequently has limited access to information about the target’s assets, in which case the presumption would impose unnecessary hurdles that could make it more difficult for the offeror to complete the transaction.

Paragraph 3.12 of the *Draft Guidelines* indicates that mix and match divestiture packages will not be typical, and that “it will normally be preferable for all the assets to be provided by one of the merger parties.” The Sections request some clarification on this point to provide some illustrative, non-exhaustive, examples of circumstances in which the CC is likely to conclude that competition risks would arise from mix-and-match divestitures, and contrasting circumstances in which such risks are unlikely to arise. For example, it would be beneficial if the *Guidelines* explained that, where different markets have several different competitive overlaps (either different product markets or different geographic markets) so that the remedy in each market is in effect independent, a divestiture of one party’s assets to remedy the substantial lessening of competition in one market and a separate divestiture of the other party’s assets to remedy the substantial lessening of competition in another market ordinarily should present no issue. In fact, such approaches are regularly permitted by the US antitrust authorities and aren’t generally considered mix-and-match packages, a term reserved for packages that include assets from both parties in one or more discrete markets.

The Sections note that the CC’s position on alternative divestiture packages has evolved since the 2004 Guidelines. The *Draft Guidelines* appropriately weigh the costs and benefits of requiring alternative divestiture packages and recognize the potential for “regulatory gaming” that such packages can induce from potential divestiture buyers. We agree with the *Draft Guidelines*’ position that alternative asset packages may be appropriate where “there is doubt as to the marketability of the initially proposed divestiture package or where a business is subject to major asset risks and speed of divestiture is likely to be a critical requirement.” *Draft Guidelines* ¶ 3.13. However, the

⁸ For example, in many ordinary course pharmaceutical transactions, product rights are sold through licensing and asset sales, frequently without the need to divest plant and equipment, R&D and sales organizations.

Draft Guidelines do not explain whether such concerns may also be dealt with by identifying an acceptable up-front buyer. The Sections welcome the fact that, unlike the 2004 Guidelines, the *Draft Guidelines* do not favor alternative divestiture packages in the form of so-called crown jewel provisions. The Sections submit that the use of crown jewel provisions is unsound policy in many cases, as such provisions often distort the incentives of the merging parties and the divestiture buyers as well as potentially imposing significant welfare losses, and the potentially punitive nature of crown jewel provisions would likely violate the *Draft Guidelines*' core principle of proportionality.

Although these comments discuss mix-and-match, upfront buyers and alternative assets packages as separate points, in practice the U.S. antitrust agencies view all these points to be interrelated aspects to be considered in defining appropriate divestiture packages. That is, if the package being discussed is not stand-alone, the agencies may require an upfront buyer, to reduce what the *Draft Guidelines* describe as composition risk. Similarly, the presence of a thoroughly vetted upfront buyer generally reduces, if not eliminates, the need to define an alternative package. Indeed, it might be noted that the increased use of upfront buyers in the U.S. has coincided with a decrease in alternative asset packages or crown jewel provisions.

With respect to the criteria for suitable purchasers, the Sections agree that the four criteria set out in paragraphs 3.15 to 3.17 are the appropriate criteria. However, certain criteria might benefit from further refinement. For example, the *Draft Guidelines* do not indicate how "reciprocal trading relationships" would affect the assessment of the independence of a purchaser. In the Sections' view, the CC should exercise great care to ensure that trading relationships that are common, arms-length commercial relationships are not automatically deemed problematic. Similarly, the Sections respectfully submit that requiring a complete "absence of competitive or regulatory concerns" sets too strict a standard for divestiture buyers.⁹ This criterion could be interpreted to mean that divestitures to existing market participants would be

⁹ This appears similar to the EC's requirement that the purchaser present no prima facie competition problems. Notice on remedies acceptable under Regulation (EEC) No. 4064/89 and Regulation (EC) No. 447/98 (OJ 2001 C68/03) at ¶ 59 (Mar. 2, 2001) ("Where the Commission determines that the acquisition of the divestiture package by the proposed purchaser, in the light of the information available to the Commission, threatens to create prima facie competition problems or other difficulties, which may delay the timely implementation of the commitment or indicate the lack of appropriate incentives for the purchaser to compete with the merged entity, the proposed purchaser will not be considered acceptable.").

disfavored against divestitures that create an entirely new market participant. The Sections' comments on the 2004 Guidelines noted that such decisions often involve a tradeoff. The viability risk is often lower in the case of divestiture to an existing market participant, because the existing market participant typically has some knowledge and experience in the industry and is often only lacking a critical scarce asset in order to compete effectively. Similarly, although divestiture to a buyer who is not an existing market participant could be seen as potentially enhancing competition, such divestitures often entail a higher degree of viability risk and may require the package of divestiture assets to be substantially larger than those that would be necessary in the case of a divestiture to an existing market participant.

Paragraph 3.17 of the *Draft Guidelines* provides that where more than one party may be interested in purchasing the divestiture assets, "the CC will generally wish to evaluate whether purchasers fulfill the criteria before any purchaser is granted exclusivity to undertake detailed due diligence." The Sections submit that, in some circumstances, these are risks that sophisticated commercial parties should be able to manage without direct CC involvement. In such circumstances, the CC should avoid becoming actively involved in the process of due diligence and sale, particularly as the merging parties will often have a legitimate interest in, and a fiduciary obligation to ensure, a competitive auction to maximize the proceeds from the sale of the divestiture assets, whereas potential buyers will typically have an incentive to game the regulatory process to their commercial advantage in any auction.

Paragraph 3.23 of the *Draft Guidelines* provides that the CC will normally require a monitoring trustee to oversee the parties' compliance with undertakings. As stated in our comments on the 2004 Guidelines, the Sections believe that although special circumstances may require a monitoring trustee (for example, if the assets would otherwise likely be wasted), generally it should not be necessary to appoint a monitoring trustee to oversee the divestiture process. In the Sections' experience, monitoring trustees can add substantially to the compliance burden and costs of remedial action, often without any perceptible impact on the outcome of the remedy. Moreover, the Sections believe that U.S. experience shows that compliance usually can be effectively monitored through ongoing reporting obligations and appropriate supervision by the enforcement authorities.

With respect to divestiture trustees, the Sections observe that provisions for the appointment of a divestiture trustee in the event that the divestitures have not been effected after a certain period are commonplace in DOJ and FTC consent decrees. However, Paragraph 3.26 of the *Draft Guidelines* provides that the CC may require the appointment of a divestiture trustee at the outset of the divestiture process if the CC has reason to suspect the parties would not be able to procure a buyer within the divestiture period. The Sections question the need for such a provision and note that no similar provision has been employed by the U.S. enforcement agencies. Although the *Draft Guidelines* note that this would occur only in “unusual cases”, the Sections suggest that such concerns might be more effectively dealt with through other provisions (such as requiring sale to an acceptable up-front buyer in situations where there are substantial doubts as to the parties’ ability to complete an appropriate divestiture).

The Sections agree broadly with the *Draft Guidelines*’ discussion of intellectual property remedies and concur with the CC’s assessment that such remedies may often be viewed “as a specialized form of asset divestiture.” *Draft Guidelines* ¶ 3.28. However, the Sections question why paragraph 3.30 concludes that “the CC will generally prefer to divest a business including IP rights, where this is feasible, rather than rely on IP remedies alone.” The Sections suggest that the *Draft Guidelines* could be clarified to provide further detail regarding those situations where the divestiture of an IP right will be an acceptable remedy. For example, in some cases, the only scarce asset necessary to restore competition may be intellectual property such as a trade secret, know-how, patent, or copyrighted information. In such cases, a divestiture of the necessary IP rights to a buyer that already has the other, non-scarce assets, or can easily obtain them from third parties, would typically be sufficient to restore competition. In the Sections’ experience, such cases arise sufficiently frequently to render a presumption in favor of divesting an entire business inappropriate.

Conclusion

The Sections believe that the *Draft Guidelines* represent a sophisticated statement of enforcement practices and policies, but respectfully submit that revisions consistent with our recommendations in these comments would provide valuable additional guidance that will benefit consumers, parties to concentrations and competitors in affected industries, as well as the CC itself. The Sections appreciate the opportunity to

provide comments on the *Draft Guidelines* and commend the CC for its continued work in updating and revising its guidelines.