THE ROLE OF CONDUCT REMEDIES IN ADDRESSING MERGER COMPETITIVE EFFECTS

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While antitrust agencies long have preferred structural remedies, the U.S. Department of Justice (DOJ) recently has shown a new willingness to use conduct remedies in merger enforcement.[2] Conduct remedies constrain the post-merger behavior of the merged firm. They may be used alone or combined with a structural remedy. DOJ's 2011 "Policy Guide To Merger Remedies" is much more favorable to conduct remedies than the 2004 Guide. The 2004 Guide described conduct remedies as typically "more difficult to craft, more cumbersome and costly to administer, and easier. . . to circumvent" than structural remedies.[3] In contrast, the 2011 Guide describes these remedies as a "valuable tool" to preserve a merger's efficiencies while eliminating its competitive harm.[4] Conduct remedies provide the antitrust authorities with a more flexible response to perceived threats to competition, but they also raise a number of serious issues. Studies by both the Canadian Competition Bureau (CCB) and the European Commission's Directorate General for Competition (DG-Competition) of conduct remedies in past mergers present at best a mixed picture of their effectiveness.[5]

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[1] Vice President, Economists Inc.

[2] See Jeremy J. Calsyn and Patrick R. Bock, "Merger Control Remedies: A More Flexible Administration," *Antitrust,* vol. 24, No. 3, Summer 2010, at 15-19.

[3]U.S. Department of Justice Antitrust Division, "Antitrust Division Policy Guide to Merger Remedies," October 2004, p. 8, available at http://www.justice.gov/atr/public/guidelines/205108.pdf.

[4] U.S. Department of Justice Antitrust Division, "Antitrust Division Policy Guide to Merger Remedies," June 2011, at 6-7. (hereinafter*2011 Remedy Guide*), available at http://www.justice.gov/atr/public/guidelines/272350.pdf .

[5] Competition Bureau of Canada, "Merger Remedies Study," August 11, 2011. (hereinafter*CCB Study*), available at http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/vwapj/cb-merger-remedy-study-summary-e.pdf/$FILE/cb-merger-remedy-study-summary-e.pdf ; European Commission's Directorate General for Competition, "Merger Remedies Study," October 2005.

Conduct remedies are typically used to address perceived problems with vertical mergers and with the holding of minority interests, although in some cases they may be used in horizontal mergers.[6] The 2011 Guide describes a variety of different conduct remedies.[7] Their application is perhaps best illustrated by their use in several recent mergers.

Conduct Remedies in Five Merger Consent Orders

Google-ITA: By acquiring ITA, Google would gain control of QPX, a software product that DOJ viewed as a critical input into travel search web sites. Google was planning to launch such a web site itself, and DOJ feared that Google might have the incentive to foreclose its competitors, some of which had existing licenses to use QPX. Thus, the remedy required Google to continue existing QPX licenses, to renew those licenses under similar terms and conditions, and to license QPX to new customers under fair, reasonable and non-discriminatory terms. Google was also required to continue to improve QPX. Google was also required to establish internal firewalls to ensure that competitively sensitive information that it received from supplying QPX to its competitors was not used to disadvantage those firms.[8]

Comcast-NBC Universal: Comcast and NBC Universal agreed to contribute all their programming assets to a joint venture that would be 51% owned by Comcast. DOJ feared that Comcast could use its control of a joint venture that owned valuable programming to prevent the entry and growth of

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(hereinafter*DG-Competition Study*), available at http://ec.europa.eu/competition/mergers/legislation/remedies_study.pdf .

[6] "Joint Comments of the American Bar Association's Section of Antitrust Law and Section of International Law on the Competition Bureau (Canada) Draft Information Bulletin on Merger Remedies in Canada," February 24, 2006, at 4.

[7] *2011 Remedy Guide* at 12-28.

[8] "Competitive Impact Statement," U.S. v. Google Inc. and ITA Software, Inc., No. 1:11-cv-00688 (D.D.C., *filed* April 8, 2011), available at http://www.justice.gov/atr/cases/f269600/269620.pdf (hereinafter *Google CIS*).

firms that might compete with it in video distribution.[9] Of particular concern was the acquisition's effect on online video distributors, a group of new entrants into video programming distribution. As a remedy, the parties were required to license programming to those distributors.[10]

Live Nation-Ticketmaster: DOJ feared that Ticketmaster's acquisition of the best-positioned new entrant would reduce competition in the market for primary ticketing services for major concert venues. The remedy included requiring Ticketmaster to take steps to facilitate entry by a third firm, AEG. Specifically, Ticketmaster was required to provide AEG with a web site for providing ticketing services based on Ticketmaster's technology but with AEG's brand. Moreover, for four years, Ticketmaster was required to provide AEG an option to acquire a fully paid-up license to the then-current version of Ticketmaster's platform, including the source code. Ticketmaster would have to install that platform and provide six months of technical assistance. The web site would be provided for up to five years. To give AEG an incentive to establish a ticketing business that was fully independent of Ticketmaster, either by licensing the Ticketmaster platform or in some other way, Ticketmaster was forbidden to provide primary ticketing services to AEG venues after the end of that period. In addition, Ticketmaster was required to establish another independent competitor by divesting assets to Comcast-Spectacor, and it was forbidden from engaging in certain practices that might stifle the growth of its competitors. For example, it

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[9] "Competitive Impact Statement," U.S. and Plaintiff States v. Comcast Corp., *et al.,* No. :11-cv-00106 (D.D.C. *filed* January 18, 2011), available at http://www.justice.gov/atr/cases/f266100/266158.pdf (hereinafter *Comcast CIS*). This merger also fell under the jurisdiction of the Federal Communications Commission. For a discussion of that agency's consideration of the merger, see Jonathan B. Baker, "Comcast/NBCU: the FCC Provides a Roadmap for Vertical Merger Analysis," *Antitrust,* vol. 25, no. 2, Spring 2011, at 36-42.

[10] The parties also were required to relinquish governance and voting rights stemming from their partial ownership of Hulu, an on-line video distributor. *Comcast CIS* at 11.

was not allowed to use ticketing data in its non-ticketing business unless it also gave that data to other promoters and managers.[11]

*GrafTech-Seadrift:*GrafTech International, a manufacturer of graphite electrodes, acquired Seadrift Coke, a producer of needle coke, the major input into electrode production. GrafTech did not produce needle coke, but it had supply contracts with Conoco, the other major producer of needle coke, and those contracts involved a significant exchange of pricing and cost information between the parties. DOJ feared that the information exchange would make collusion easier, thus leading to coordinated interaction. The remedy was to eliminate the information sharing provisions in the contract and to prohibit GrafTech from entering into other contracts with Conoco that had such provisions.[12]

In the Matter of PepsiCo, Inc.: PepsiCo acquired all outstanding voting securities and equity interests in two of its bottlers.[13] Those firms also bottled concentrate provided by one of PepsiCo's competitors, Dr. Pepper Snapple Group (DPSG). Concentrate manufacturers provide their bottlers with competitively sensitive information, and the FTC feared that PepsiCo might use this information either to gain unilateral market power or to facilitate coordinated interaction in various markets for concentrate. The remedy was a firewall that prevented

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[11] Also, Ticketmaster was notallowed to require venues that scheduled its concerts or artists to use its ticketing services, and it had to provide any ticketing clients with their ticketing data upon request. The last requirement was to make it easier for customers to switch ticketing suppliers. "Competitive Impact Statement," *U.S. v. Ticketmaster Entertainment Inc. and Live Nation, Inc.*, No. 1:10-cv-00139 (D.D.C., *filed* January 25, 2010) (hereinafter *Ticketmaster CIS)* (available at http://www.justice.gov/atr/cases/f254500/254544.pdf).

[12] "Competitive Impact Statement," *U.S. v. GrafTech International Ltd., and Seadrift Coke, L.P.,* No. 1:10-cv-02039, D.D.C., *filed* November 29, 2010 (hereinafter *GrafTech CIS*) (available at http://www.justice.gov/atr/cases/f264600/264608.pdf).

[13] It already owned substantial minority interests in those firms. PepsiCo later acquired the outstanding ownership interests in a third smaller bottler. "Complaint," *In the Matter of PepsiCo,* September 27, 2010.

PepsiCo employees with "concentrate related functions" from accessing DPSG's information.[14]

Four of these five mergers were essentially vertical transactions. The fifth, Ticketmaster-Live Nation, involved the acquisition of the most likely potential entrant but also involved questions concerning vertical relationships. In three instances, the primary concern was that the merged firm would control assets that its competitors needed to access to be able to compete, and the remedy involved guaranteeing that access. In these three cases, the asset involved intellectual property, and the access was a license, but conduct remedies may involve other types of access. For example, these remedies may include supply agreements.[15] In two instances, the primary concern was that the merged firm would have competitively sensitive information concerning a major competitor, and the remedy eliminated or restricted the firm's access to that information. Information restrictions were also applied in two of the cases where the remedy involved guaranteed access. This article will concentrate on access guarantees and information restrictions as those recently have been the two most important types of conduct remedies.

Difficulties Inherent In Guaranteeing Market Access

1. Setting Price and Terms

Implementing access guarantees raises a number of issues, the most serious of which is the problem of how to set the price and terms of the access. If the price is set too high or the terms are too onerous, then the relief may be ineffective. If the price is too low or the terms too generous, then there may be inefficient use of the assets involved. The DGComp study states, "The primary

[14] "Analysis of Agreement Containing Consent Order to Aid Public Comment," *In the Matter of PepsiCo,Inc.,*FTC File No. 091 0133 (*filed* February 26, 2010) (available at http://www.ftc.gov/os/caselist/0910133/100226pepsicoanal.pdf).

[15] *2011 Remedy Guide* at 17.

causes for the failure of access commitments were found to lie in the inherent difficulties in setting the terms for effective access and in monitoring them."[16]

One suggested solution to this problem is to require that the price and terms of access be based on competitive benchmarks. For example, prices charged competitors may be based on those charged to other customers that the merged party does not compete with and thus has no desire to foreclose. Prices also may be based on those available from other firms that provide products that are very similar to those provided by the merged entity. Alternatively, prices and terms may be based on the levels that prevailed before the merger.

The consent decrees described above that involved guaranteed access use these approaches. In the *Comcast* decree, on-line distributors must be allowed two options for acquiring programming from the joint venture. First, they will be able to license programming at the same terms available to multichannel video programming distributors. As Comcast does not compete with many of those distributors, those terms may be good proxies for competitive terms. Second, they will be allowed to license programming from the joint venture that is "comparable in scope and quality" to the programming that they receive from one of the joint venture's "programming peers."[17]

The other two consent decrees both use pre-merger benchmarks. In the *Ticketmaster* consent decree, the royalty that Ticketmaster may charge AEG for tickets sold using the web site is set below Ticketmaster's average pre-merger rate.[18] In the *Google* consent decree, Google is required to renew licenses for QPX at terms and conditions that are similar to those that existed before the merger. If an online travel intermediary does not already have a license to QPX, then Google must offer it terms that are "fair reasonable, and non-discriminatory,"

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[16] *DG-Competition Study* at 165.

[17] *Comcast CIS* at 10.

[18] *Ticketmaster CIS* at 14.

compared to those offered "similarly situated entities," which likely would include entities with licenses concluded before the merger.[19]

2. Quality Issues

Guaranteeing access requires not only that reasonable prices and terms be established but also that the quality of the asset involved be maintained. That is a particularly serious problem in high-technology industries, where the technology being offered to competitors may be allowed to lag behind that of the merged entity, thus putting the competitors at a serious disadvantage. In the Google consent decree, that problem was addressed by requiring Google to continue to develop "ordinary course upgrades and enhancements" to QPX and to devote "substantially as many resources to research and development for QPX as ITA did prior to the acquisition."[20] Thus, the pre-merger level of effort was used as a benchmark to determine what would be appropriate post-merger.

The success of these approaches to the issues of prices and terms of access and quality of assets remains to be seen. Often, guaranteeing access requires setting a wide variety of terms and conditions. Moreover, the competitors receiving access may vary widely in their use of that access and in the cost the acquirer incurs in serving them. Thus, it may be very difficult to determine if the terms under which any given firm is offered access are consistent with the consent decree. For example, the *Comcast* consent decree requires the joint venture to offer an online video distributor a license that "must reasonably approximate, in the aggregate, an existing licensing agreement. That approximation must account for factors, such as advertising revenues and any technical and economic

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[19]*Google CIS* at 3.

[20]*Id.* If Google's revenues from the third party licensing of QPX fall, then it may, with DOJ consent, be allowed to reduce resources devoted to research and development for QPX. "Final Judgment," U.S. v. Google Inc. and ITA Software, Inc., No. 1:11-cv-00688 (D.D.C., *filed* October 5, 2011) (available at http://www.justice.gov/atr/cases/f275800/275897.pdf) at 16.

limitations of the OVD seeking a license."[21] Determining whether one license reasonably approximates another may be very difficult. Similarly, it may be very difficult to determine what "ordinary course upgrades and enhancements" to software would be in the absence of a merger.

Access guarantees likely will require ongoing monitoring, and such monitoring can be extremely important to the functioning of the remedy. The CCB study found evidence that a failure to appoint monitors reduced the effectiveness of conduct remedies.[22] Moreover, disputes over the application of the remedies may involve the agencies and the merged firm in continuing litigation that could go on for years after the merger. The *Google* and *Comcast* consent decrees both have provisions that allow firms that believe they have not been granted access under appropriate conditions to apply to DOJ for permission to begin binding arbitration.[23] Not only do such provisions raise the prospect of further disputes and dispute resolution, they may not always be effective. The CCB study found that in some cases formal arbitration methods were difficult to use.[24]

3. Duration of Access

Another serious issue with access guarantees, as with all conduct relief, is their duration. Different antitrust authorities take different approaches to setting the duration of remedy. The United Kingdom's Competition Commission may have the remedy last only a short period if the Commission believes that the remedy need only be effective in a transitional period. If the remedy must apply for as long as the lessening of competition from the merger persists, then the Commission will not set an expiration date for the remedy, as the necessary

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[21] The FCC's order pertaining to this transaction also has an arbitration provision, and DOJ will typically defer to the FCC's arbitration, but it also retains the right to require use of its own arbitration provision. *Comcast CIS* at 1, 10.

[22] *CCB Study* at 7.

[23] *Comcast* CIS at 12; *Ticketmaster CIS* at 10.

[24] *CCB Study* at 7.

duration will not be predictable. Instead the Commission will rely on the merged company to apply for a change of relief if circumstances change.[25] DOJ's remedy guide does not discuss the typical duration of conduct remedies, but access guarantees imposed in recent cases expire after a set number of years. The final judgment expires in five years in the *Google-ITA* case, seven years in the *Comcast-NBC* case, and ten years in the *Ticketmaster* case.[26]

The appropriate goal would be for conduct relief to last until changes in the market mean that it is no longer required, but it is difficult or impossible to predict how long that will be. Too short a remedy period may mean that relief is insufficient. The CCB study notes that "unless underlying structural change occurs in a market prior to the expiry of the remedy, there are no constraints on the merged firm to exercise market power thereafter."[27]

A lengthy relief period also poses risks. Markets may undergo a variety of changes that cannot be predicted at the time of the merger and that may affect the desirability and effectiveness of relief. The European experience indicates how significant such changes may be. The DGComp study analyzed four cases involving remedies that guaranteed access to infrastructure. In three of those cases, the markets involved developed in a way that was very different from what had been expected at the time of the merger, and as a result the remedy proved to be unnecessary.[28] Changes in the markets may be a particularly serious problem if pre-merger benchmarks are used in the pricing of access. As time passes and

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[25] The Commission may set a "long-stop date" after which relief will not apply. UK Competition Commission, "Merger Remedies: Competition Commission Guidelines," November 2008, ¶ 4.7 (available at http://www.competition-commission.org.uk/rep_pub/rules_and_guide/pdf/cc8.pdf).

[26] "Final Judgment," *U.S. v. Google Inc. and ITA Software, Inc.,* No. 1:11-cv-00688 (D.D.C., *filed* October 5, 2011 (available at http://www.justice.gov/atr/cases/f275800/275897.pdf) at 33; "Final Judgment," *U.S. and Plaintiff States v. Comcast Corp., et al.*, No. 1:11-cv-00106 (*filed* September 1, 2011) at 32 (available at http://www.justice.gov/atr/cases/f274700/274713.pdf); "Final Judgment," *U.S. v. Ticketmaster Entertainment Inc. and Live Nation, Inc*., No. 1:10-cv-00139 (*filed* July 30, 2010at 26).

[27] *CCB Study* at 8.

[28] *DG-Competition Study* at 115.

markets change, the information in those prices may become less useful in estimating what prices would be under competition.

4. Conclusion Concerning Access Guarantees

Given these difficulties, guarantees of access should rarely if ever be used as a remedy in merger cases. If a merger promises substantial efficiencies but also threatens substantial anticompetitive effects, access guarantees may appear a better option than blocking the merger completely or allowing it without conditions. Nevertheless, because of the difficulties inherent in implementing access guarantees, there will be few if any mergers where they are the best option. This view is consistent with the findings of the DG-Competition Study. That study finds that such remedies "have only worked in a very limited number of instances," due to "inherent difficulties" in setting and monitoring the terms of access.[29] The study concludes that the use of these remedies should be limited to cases where these difficulties can be minimized.[30]

Information Flow Restrictions

Conduct remedies that restrict the flow of information, either by limiting contracts, as in *GrafTech*, or by erecting firewalls post-merger, as in *PepsiCo*, appear less problematic.[31] Nonetheless, these remedies also have some disadvantages. These restrictions may complicate business operations and block efficient contracts. If merger-related efficiencies depend on better coordination of vertically-related segments of the merged firm, these restrictions may block the information flows required for such coordination and thus prevent the firm from realizing those efficiencies.

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[29] *DG-Competition Study* at 165.

[30] *Id*.

[31] Restrictions on information flows were also part of the remedy in the *Ticketmaster* and *Google-ITA* matters, as noted above. In addition, such constraints were used in earlier cases. See *2011 Remedy Guide* at19 & n. 31.

These restrictions may also be difficult to monitor to ensure compliance. If a merged firm denies a competitor access in violation of a consent decree, then the competitor will know of the denial and have an incentive to complain to the antitrust authorities. If a merged firm violates a restriction on information sharing, the violation may be difficult for either the intended beneficiaries of the information barriers or competition enforcement agencies to detect. Moreover, restrictions on information sharing are often put in place to limit coordinated interaction. As the firm's competitors would likely benefit from the coordinated interaction, they would have no incentive to report the violation. Thus, restrictions on information sharing may be harder to enforce than access requirements. The European experience with these remedies indicates that they require substantial post-merger monitoring.[32] In considering conduct remedies, antitrust authorities should consider whether they will have sufficient resources for such monitoring.

As with access guarantees, the duration of information restrictions must be determined. The U.S. antitrust authorities also typically set a fixed expiration date for these restrictions. The remedies in *GrafTech* apply for ten years, the remedies in *PepsiCo* for twenty.[33]

Conclusion

The use of conduct remedies raises a number of serious issues, and it may be difficult or impossible to use these remedies as the basis for a competitively desirable relief. Thus, the antitrust authorities should make at most only a limited use of these remedies and should continue to prefer divestiture. Moreover, the U.S. antitrust authorities should pay careful attention to how these remedies

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[32] Nicolas Petit, "Remedies For Coordinated Effects Under The European Union Merger Regulation," University of Liege, 2010, *available at* *http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1639906*at 7. The DG-Competition Study does not review information restrictions.

[33] "Final Judgment," *U.S. v. GrafTech International Ltd., and Seadrift Coke, L.P.*, No. 1:10-cv-02039 (D.D.C., *filed* March 24, 2011) at 10 (available at http://www.justice.gov/atr/cases/f268900/268995.pdf); "Decision and Order," *In the Matter of PepsiCo,* Inc., FTC File No. 091 0133 (*filed* February 26, 2010) (available at http://www.ftc.gov/os/caselist/0910133/100226pepsicodo.pdf) at 12.

function in the various instances where they were recently applied. A review of the experience with conduct remedies in those mergers may be extremely valuable in determining the appropriate use of such remedies in the future.