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The 2023 Merger Guidelines: A Critical Assessment

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Economic thinking evolves in light of new evidence, experience, and theoretical developments as to how to evaluate mergers. It is therefore useful for the government agencies to update Merger Guidelines from time to time to reflect that new economic knowledge. The Guidelines have been updated in the past on a few occasions; the previous revision was in 2010.[1] Of course, there are always some points on which there can be disagreement, but I think it is fair to say that the Guidelines have served as a useful statement of economic thinking that merging parties have looked to and courts have relied upon in how they can use economic reasoning to evaluate evidence that bears on the likely effects of a merger.

Although I applaud the agencies' effort to update the Guidelines and appreciate the efforts of the drafters to listen to and incorporate at least some comments that I and many others raised with respect to the Draft Guidelines, there are several features of the 2023 Guidelines that I dislike as I explain in more detail in this article.

My main complaint is that the radically altered form of the 2023 Guidelines compared to prior Guidelines has transformed them from an economic guide on how to interpret evidence into a legal guide of how the enforcement agencies interpret the antitrust laws with regard to mergers and how the enforcement agencies will litigate an antitrust case that challenges a merger. I fear that this altered form will rob the Guidelines of what they have become: a durable guide to economic thinking.

Although I am critical of the altered form of the 2023 Guidelines, I do appreciate some of the analyses of economic issues that prior Guidelines had omitted. This is

[1] I exclude from my discussion the short-lived Vertical Merger Guidelines (2020), which were withdrawn soon after their appearance.

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not the place for an in-depth discussion of the many economic issues in the prior and new Guidelines, since they have been extensively discussed over the years by me and many others. Instead, I will focus on a few high-level points.[2]

Section 1 of this paper begins my critique of the altered form of the 2023 Guidelines with its extensive case citations and implied interpretations. I explain why the very structure of the 2023 Guidelines, which is based on establishing a prima facie case followed by rebuttal, is not necessarily a good model for economic analysis – either before the agencies or in court, even if in litigation attorneys may structure their legal argument in that way. Section 2 discusses the generally hostile tone to mergers and efficiencies that seem to me to permeate the 2023 Guidelines. I turn next to an analysis of several individual Guidelines. Sections 3, 4, and 5 discuss the emphasis on market definition, mergers involving potential competitors and vertical mergers, respectively. I conclude in Sections 6 and 7 with a discussion of two important issues that are missing in these (and prior) Guidelines. There is a lack of recognition of the ability of private contracts to eliminate alleged harms, and an absence of any sense that the agencies will follow up on their decisions as to whether to challenge or not challenge a merger to see whether their theories and empirical predictions, as well as those of the parties involved, materialized.

1 Stress on Legal Cases Rather than Economic Analysis Threatens the Durable Nature of the Guidelines

The 2023 Guidelines represent a significant departure from past Guidelines. The 2023 Guidelines succeed in conveying the more aggressive antitrust policy of the current administration. They justify this more aggressive posture by citing numerous legal cases.[3] By turning the Guidelines into a guide for how the current administration thinks antitrust law should be interpreted, the 2023 Guidelines detract attention from what had been their main purpose: an explanation of what an evidence-based economic analysis requires.

To put this point into perspective: There are over 70 citations to cases in the new Guidelines. The number of case citations in the 2010 Guidelines and prior Guidelines is zero! This emphasis on case citations and the suggested interpretations may serve the goals of this administration in their efforts to influence courts; but my hunch, though I am not a lawyer, is that there will be much dispute as to whether the cases that are cited for various principles in the 2023 Guidelines accurately convey current antitrust law. And then, if I am correct, this dispute will taint how the 2023 Guidelines are received. I would not be surprised if courts reject some of the case interpretations that are contained in the 2023 Guidelines; and subsequent

[2] For some of my recent analyses of issues that are related to the 2010 Guidelines and 2023 Draft Guidelines, see Carlton and Israel (2010, 2021) and Carlton (2023a, 2023b). For a review of the 2010 Guidelines and 2023 Draft Guidelines by several other authors, see the February 2021 issue of *Review of Industrial Organization* and the ProMarket (2023).

[3] They also refer to "the collected experience of the Agencies…and…the public consultation process" (p. 4). It is unclear what experience they are referring to. I will discuss the importance of this point below.

administrations may well issue new Guidelines when they come into office to reflect their own preferences for how they interpret the antitrust law.

It is appropriate for an administration to inform the public as to how aggressive it will be in its enforcement of the antitrust laws so that businesses can act accordingly. But if every administration issues its own Guidelines, the reputation of the Guidelines as a durable guide to economic thinking will be undermined as will the idea that merger policy should be based on economic analysis.

It is precisely this concern that motivated me and 16 other former Chief Economists at the FTC and Department of Justice—of both Democratic and Republican administrations—to warn against using the Guidelines to cite and interpret legal cases and, instead, to keep the economic analysis separate from any legal analysis or policy statement.[4] Had the enforcement agencies done that, then the economic component of the Guidelines could have remained as a document of economic reasoning, even if the administration's desired legal interpretation of antitrust principles changes over time as new political administrations come into power. Indeed, as my discussion below makes clear, my main concerns are less with the Guidelines' discussion that is focused on economic analyses (Sect. 4), than with the first three sections of the 2023 Guidelines – which I suspect will be considered the heart of the new Guidelines.

In keeping with their focus on the law, not economics, the main individual Guidelines (Guidelines 1–6) are described as how a particular merger "can violate the law". That could be an indication that the agencies are looking for mergers that trigger violations of the antitrust laws as the agencies interpret them rather than, for example, mergers that harm competition, thereby reducing consumer (including, where relevant, input suppliers') welfare.[5] This might seem like a minor point to many; but to me it indicates that the agencies could be focused on whether they can win in court, not whether the merger actually harms competition.[6]

If there is a poorly decided Supreme Court case, would the enforcement agencies bring a case even if there is no actual harm to competition but they could win in court based on that poorly decided precedent? I hope not and would not expect the enforcement agencies to act in that way. But to remove any such concerns, I would have liked to have seen in the individual Guidelines a replacement of the phrase

[4] Baker et al. (2023).

[5] I cannot tell whether the Guidelines endorse or reject the idea that a harm to competition is a harm to the competitive process that results in a decline in consumer (including where relevant, input suppliers') welfare, as that term has been interpreted for many years. In light of pronouncements from agency officials where additional goals have been suggested, it would be useful for the agencies to clarify in a separate statement that the economic welfare of consumers (including, where relevant, input suppliers) will remain the focus of enforcement actions, and that other goals such as fairness (undefined), reduced income inequality, the promotion of democracy, or other worthy goals will not enter the decision-making with regard to antitrust enforcement actions. It is not that these other goals are not worthy ones; but an antitrust policy that lists multiple goals that can conflict with each other, but provides no method for making trade-offs among them, risks turning antitrust enforcement policy into an arbitrary, highly subjective process.

[6] I note that some of the cases that are cited for various antitrust "principles" often involve situations at which economists today would cringe if they were told that those cases represented a harm to competition. See, e.g., Hovenkamp (2023a,b).

"can violate the law" with a statement that the agencies will attack only mergers that "can harm competition".

2 The 2023 Guidelines Appear to be Hostile to Mergers and Efficiencies

Perhaps it is just me; but my initial reaction to the 2023 Guidelines is that they are openly hostile to mergers, and they cite statutes and cases to support that view. The Introduction stresses that the purpose of merger enforcement is to prevent a merger whose effect "*may* be to substantially lessen competition". I understand that the quote is from a decision citing the words in the Clayton Act, but the interpretation of that clause is a subject of many court decisions. I do not think it accurate to claim that the mere possibility of competitive harm, however remote, is enough to stop a merger under the antitrust laws, but I will leave that to the legal scholars to deny or confirm.

However, in interpreting the Clayton Act, the 2023 Guidelines chose to cite a case where the word "may" is italicized even though it does not appear that way in the Clayton Act. And, just before the reader is being instructed how to use the 2023 Guidelines, the reader is reminded that the agencies use a variety of tools to determine whether the merger "may" harm competition. Finally, at the start of Sect. 4's discussion of rebuttal evidence, the 2023 Guidelines remind the reader that the relevant legal standard is whether the merger "*may*" —again italicized—harm competition.

The hostility toward mergers is reflected in what appears to be little recognition that mergers can generate efficiencies and thereby benefit competition. There is no sentence in the Introduction acknowledging that mergers can enhance competition, although that should be obvious from the fact that only a small fraction of all mergers are considered by the agencies to be anticompetitive. In keeping with the legal framework of the prima facie case that ignores efficiencies, the discussion of efficiencies comes in only as rebuttal evidence that is described later on in Sect. 3 of the Guidelines, where the reader is cautioned that the agencies will be skeptical of those efficiency claims.

I would have preferred an introduction such as:

> "Merger transactions are common in our economy. They occur in a large majority of cases to improve the efficiency of the firms involved, as those firms see matters, and raise no competition issues. Instead they promote competition and bring benefits to our economy. However, some mergers can harm competition and thereby harm our economy. It is the task of the government agencies to prevent the undesirable mergers without removing the incentives to engage in the desirable ones. The purpose of these Guidelines is to inform businesses how the government agencies evaluate evidence in order to decide whether a proposed transaction raises a significant risk of harm to competition. This discussion is rooted in the use of economics to analyze evidence including data, business documents and testimony."

Notice two things about this paragraph: First, it agrees that some mergers can harm competition, but also recognizes the indisputable fact that most mergers promote efficiency and do not raise antitrust issues. Second, it says nothing about what the antitrust laws compel and sticks to explaining the economic interpretation and analysis of evidence. The 2010 Guidelines, as well as prior Guidelines, would, I think, be compatible with this paragraph.

Moreover, nothing in this paragraph prevents increased aggressiveness in preventing mergers compared to prior years, when the economic evidence of past transactions lends support for more aggressive action: Even if no tools of economic analysis have changed since 2010, there is nothing in that paragraph or in the 2010 Guidelines that would prevent an agency from stating, for example, "We have reviewed lots of past mergers; and, in the majority of cases where the possibility of entry was claimed to constrain future price increases, we find that entry failed to materialize with the result that prices rose post-merger. Hence we will reduce the weight we place on such claimed entry as a constraint on pricing post- merger." Or: "We have reviewed past mergers and find that the majority of the mergers that we did not challenge raised prices when the HHI and its change exceeded certain levels. Accordingly, we will scrutinize such mergers more carefully."

Well, who cares how Carlton would have written the opening paragraphs? If you read the 2023 Guidelines in their entirety, these Guidelines do not deny that there can be efficiencies. But that now leads me to another point as to why I dislike several features of the 2023 Guidelines: The 2023 Guidelines make clear that an analysis proceeds first by establishing a prima facie case of harm. Then the parties can rebut that presumption with claims of efficiencies or other claims. Then the weight of those competing claims is evaluated.

While this might be how a court would require expert testimony to be structured or how a court might reason, it is not a natural way for economic analysis to be done. One cannot evaluate the competitive effect of a potentially harmful merger without understanding and incorporating efficiencies into the competitive effects analysis. Lower marginal costs from a horizontal merger, for example, generate downward pricing pressure and may mean that there is no harmful effect to "offset".

Efficiencies are not simply a rebuttal point. They are part of the competitive effects analysis. Indeed, all else equal, every horizontal merger—in the absence of efficiencies—typically creates upward pricing pressure. How does that observation assist in an economic analysis? Does that create a prima facie case against every horizontal merger, no matter how unconcentrated the market? Why not, especially if any price increase, not matter how small, should matter?

One answer that recognizes the likelihood of efficiencies is that in an unconcentrated market, given that mergers generally create some efficiencies, it is unlikely that a merger will create significant harm and more likely that it will create a benefit. From an enforcement perspective, it is best to deploy scarce enforcement resources to other matters.[7] That is why there are safe harbors. But without allowing in the

[7] Enforcement decisions should generally be based on the likely harm, so that mergers in bigger markets should receive more scrutiny; see Carlton (2007a). Enforcement decisions also affect the incentive of other firms to merge. More research on this topic is needed.

analysis for some efficiencies generally from mergers, there is no reason to have safe harbors and not demand rebuttal evidence on efficiencies for every horizontal merger. And, as I will discuss below, one cannot even begin to analyze properly the effects of many vertical mergers if one ignores the consequences of the elimination of double marginalization.

I hope that the highly-trained economists at the government agencies will do a thorough economic analysis of any merger including accounting for relevant efficiencies when performing their competitive effects analysis. The fact that a legal brief to a court might require something different may be true—I defer to the legal scholars—but that should not force the economists at the agencies to twist themselves into knots and be prevented from doing a proper economic analysis as an agency evaluates the merger.

Another manifestation of the hostility to efficiencies is the statement (a variant of which appears also in prior Guidelines) that being able to achieve the claimed efficiency benefits of merger through the alternative of contract can make an efficiency not merger-specific, and therefore deserving of no credit in the merger evaluation. Although this statement is unobjectionable as a theoretical matter, we should also be asking how to evaluate claims that such contracts are likely to occur: If it is possible to achieve this benefit by contract, why haven't the merging parties already entered into such contracts pre-merger? Does the lack of such contracts pre-merger suggest that there are impediments to achieving efficiencies via contract? And shouldn't that tell us something about the likelihood that such contracts will readily be used if the merger is blocked?

There are other places in the 2023 Guidelines where the hostility to efficiencies shows up. There is, for example, a suggestion that a trend toward concentration or toward increased vertical integration could be troubling. Fair enough; but couldn't a trend toward concentration or increased vertical integration also reflect that increased concentration or vertical integration is economically efficient and pro-competitive? And isn't that what the economists or others at the agencies should try to figure out?[8] Isn't the insight of Demsetz (1973)—that increased concentration can sometimes reflect pro-competitive efficiencies—highly relevant?

The hostility to efficiencies further shows up in Sect. 3.3 of the 2023 Guidelines. To their credit, the 2023 Guidelines correctly explain that speculative and unsupported claimed efficiencies will receive little weight. It is the role of the agencies to make sure that any claimed efficiencies are credible. But this section makes no mention that past experience can sometimes help identify efficiencies. I would guess that the drafters will say in response that the 2023 Guidelines allow such evidence; but if that is what they mean to say, it would have been helpful to have it stated clearly in the efficiency section. In general, I would have preferred a more balanced discussion of the evidence that would be and would not be persuasive in evaluating efficiencies.

Section 3.3 ends with a sentence that I had to read several times to understand, and I am still not sure that I do. The 2023 Guidelines define a "cognizable efficiency" as one that, among other things, prevents a lessening of competition. Yet the

[8] Economic experts typically are not engineers or business executives, so they often have to rely on the parties for assumed efficiencies in the absence of other evidence.

last sentence of Sect. 3.3 says "Cognizable efficiencies that would not prevent the creation of a monopoly cannot justify a merger that may tend to create a monopoly." I think that means that if there are lots of efficiencies so that the price to consumers would fall post-merger, but the merger creates a firm with a market share in excess of 50% (see footnote 30 of the Guidelines), then that merger will be challenged. If that is what it means, I am not sure I understand its intent: Isn't a merger desirable if it benefits consumers?[9]

There is one final feature I find especially troubling in Sect. 3.3: the claim that harms in one market cannot be balanced against benefits in another. It is noteworthy that the famous footnote in prior Guidelines[10]—that efficiencies that are inextricably linked to the transaction can be credited in a merger analysis—has been eliminated. Does this mean that an airline merger that involves redeploying an aircraft from a small origin–destination route to a route with many more passengers, which results in a huge increase in total travel, should be illegal? Isn't that the exact opposite of how the Department of Justice has generally handled many past legacy airline mergers, though some private plaintiffs have tried and failed with that argument? If a merger benefits 1,000 workers in Chicago but harms one worker in Des Moines, are the 2023 Guidelines telling us to stop the merger? I understand the difficulties of tracing effects throughout the economy; however, for the agencies to ignore such tradeoffs and to assert that they are irrelevant in all cases is unwise.[11]

Finally, there are discussions elsewhere in the 2023 Guidelines about the importance of innovation and dynamics. Those are important topics. But if one is trying to figure out whether a merger will spur innovation or alter long-run behavior, paying attention to fixed costs is necessary – and that is nowhere discussed.[12] Usually fixed cost savings are not credited as an efficiency in merger review on the grounds that they won't affect short-run pricing. Are the enforcement agencies advocating abandoning that practice because fixed costs savings can encourage innovation? I don't know the answer; but I would have appreciated some discussion of that point given the legitimate concern over the potential effect of a merger on long-run innovation.

Let me now turn to some specific disagreements I have with some of the individual Guidelines.

3 The 2023 Guidelines, Especially Guideline 1, will Lead to an Overemphasis on Market Definition and HHI Thresholds

Guideline 1 emphasizes market definition and structural presumptions. Guideline 1 discusses a prima facie case coming from application of numerical guidelines to the calculation of an HHI based on market definition. Since it is the first Guideline, it

[9] If my interpretation is correct, it illustrates a confusion of harm to the eliminated rivals with harm to competition. See note 5 above on the definition of harm to competition.

[10] See, e.g., footnote 14 in the 2010 Guidelines. The footnote appeared first in the 1997 Guidelines.

[11] See Carlton (2023c) for further discussion of how to analyze such trade-offs.

[12] The Antitrust Modernization Commission, a bi-partisan Congressionally created committee on which I served, made this point in Antitrust Modernization Commission: *Report and Recommendations* (2007).

seems to emphasize the primacy that will be given to market definition and HHI thresholds. There is insufficient recognition in the 2023 Guidelines that market definition is at best a crude tool and one of many tools used to evaluate competitive effects. It is a place to begin – not end – an analysis, as I (and others) have written elsewhere.[13] Perhaps its best use is to create a safe harbor for mergers in unconcentrated markets; but in concentrated markets it should create at most a weak presumption of harm whose possibility should be further analyzed. At least at the agencies with their many highly competent economists, I cannot imagine market definition and HHI analysis being the primary tool used to analyze merger evidence.

Again, if one looks hard enough, one could claim that the 2023 Guidelines recognize this point (I have no doubt the agencies' economists do); but I fear that it will not be clear to other readers. And, in turn, the lack of clarity will potentially bias enforcement and court decisions even when there is convincing direct evidence of no harm in a merger that violates the HHI thresholds or conversely when there is direct evidence of harm in a merger that does not violate the HHI thresholds in a broad market.

As for reducing the HHI thresholds from the 2010 Guidelines, that is not necessarily a problem as long as everyone realizes that these thresholds and the entire exercise of market definition are crude and that their use will often provide an unreliable guide to effects of a particular merger. In Guideline 1, I am not sure what the empirical basis is for the prohibition of a 28.1% firm acquiring a firm of 2%, other than a cite to an opinion in an antitrust case—again confusing legal and economic analysis. Indeed, more generally, I have in the past criticized the lack of an empirical basis for the HHI thresholds.[14]

There are many caveats in the 2023 Guidelines that are seemingly aimed at litigation that allow the agencies to have flexibility in how they define markets. One could interpret some of the language on market definition cynically as saying that if the agencies want to do so, they will find some market definition that produces the result they want. That is likely to lead to gerrymandering market definition to obtain the desired results. If there are lots of market definitions that are "plausible" but provide different guidance as to the effect of a merger, that might that indicate that this so-called tool of analysis using market definition is unreliable in this particular

[13] See, e.g., Carlton (2007b) and Carlton and Israel (2021). As I explain in those articles, I am not in favor of abandoning market definition since I believe it can serve a useful purpose sometimes, especially in creating safe harbors.

[14] There has been a growing literature on horizontal mergers and concentration that perhaps could have been noted in the Guidelines or some associated commentary. However one views the strength of that literature (see Carlton (2020) for an evaluation), one observation is that many mergers whose shares have violated the HHI thresholds have led to price increases; but it is also true that many such mergers have led to price decreases and that ex ante it is often hard to distinguish the two possibilities. See, e.g., Ashenfelter et al. (2014). But, even if one views this evidence as showing that a violation of HHI thresholds fails to create a strong presumption of harm, it does justify increased scrutiny for mergers that raise concentration substantially in already concentrated markets.

instance?[15] Without some principles to establish which products to include in a market definition, gerrymandering is a serious concern.[16] Prior Guidelines made clear that if one is concerned about the price of product A and one includes product C in the market, then one should normally also include product B if product B is a closer substitute to product A than is product C. That principle has apparently been abandoned. I fear that such an abandonment could lead to a situation where analysts claim that they are using a hypothetical monopolist test based not on any quantitative analysis but rather on their judgment – or, even worse, that they can ignore the quantitative evidence on substitution.

There are statements about using market definition and the HHI thresholds to indicate harms from a merger because some measure of quality falls. How does this apply if quality is not viewed similarly by consumers? For example, some may like a room's temperature to be hot, while others like it cold. If the relevant quality is a room's temperature, how does one proceed in assessing whether the merger will improve or harm quality? And even if there is homogeneity of preferences among consumers, how does this analysis square with theorems in the literature that a monopolist may choose a level of quality that is the same, higher, or lower as competitive firms would choose, depending on specific assumptions? That is, even with homogenous preferences, quality is not necessarily positively correlated with concentration, all else equal. And to add even more complication, when a variety of product qualities are sold, how should one evaluate the change in the range of products produced in the context of market definition? I predict that this attempt to deal with quality in the context of market definition will in many cases lead to confusion.[17]

4 Guideline 4 Opens the Door to Speculation with Regard to Potential Entry

Guideline 4 states a simple proposition that an acquisition by a current (or future) market participant of a firm that would otherwise enter and be a significant competitor in an otherwise concentrated market is likely to harm competition. That possibility is easy to agree with theoretically. The difficult part is figuring out whether such entry is likely empirically, as well as whether the potential entrant is uniquely well-positioned to enter or merely one of many potential entrants. There has been some (but not much) work on so-called "killer acquisitions", and more work is needed.

[15] There is no debate that there can be situations where a merger of firm X and Y, all else equal, or a merger of firm Y and Z, all else equal, will each increase prices. Therefore, there are two markets that pass a hypothetical monopoly test. But now ask how one could establish this possibility. One could use merger simulation. But then what is the point of defining a market if one has already done the merger simulation that shows that either merger would be harmful? See Carlton (2007b).

[16] See Werden (2002, 2023).

[17] It is well-known that the economic analysis in many situations is not so simple as to allow one to say that competition will produce better quality, a better range of products, or better innovations than a more concentrated market structure. Nevertheless, I would view skeptically claims justifying a merger in a concentrated industry based solely on improvements along these dimensions.

My concern is that it is easy to speculate that some firm is an important potential entrant. Just as the Guidelines warn that claimed efficiencies will receive no weight if they are speculative, I would expect that the same standard would apply to claims that a firm is a potential entrant that after entry would become a significant competitor. Ever since the excellent study by Dunne, Roberts, and Samuelson (1988) that showed how rare successful entry and expansion is (and subsequent work has verified this finding—see, e.g., Foster et al. (2008)), the economics profession has been on notice not to overemphasize the ability of entry to discipline markets generally, especially in markets where entry has been rare.

Although I would like to see more research (more on this below) on how accurate are agencies' forecasts of the identity of entrants that develop into significant competitors, I would wager that it is not very good. For example, in a famous case that is cited in the 2023 Guidelines, *FTC v. Procter Gamble*,[18] the FTC prevailed in preventing P&G from buying Clorox on the grounds that P&G was a potential entrant into bleach. P&G never became a successful competitor in bleach.[19] I cite this example not because one instance proves a result but to illustrate that the blocking of that merger deprived the economy immediately of the likely efficiencies of the transaction in order to preserve a future speculative benefit from entry—a benefit that never materialized.

There are several other concerns that I have with regard to the Guidelines' treatment of evidence that would favor preventing the merger. I agree that when a potential entrant acquires an existing firm, one can and should ask whether the potential entrant is really a likely entrant. In the absence of plans to enter, speculation that "well, it is a big firm that could afford to enter" seems a weak argument – even though Guideline 4 suggests it as evidence to block a merger. Similarly, Guideline 4 discusses how it is evidence in favor of blocking the merger if the firm once evaluated de novo entry as an alternative to purchasing an existing firm. That strikes me as unbalanced unless one credits a rejection of such an entry plan also as probative. (This is a bit tricky because one needs to make sure that the rejection was not premised on buying into a concentrated industry.)

Guideline 4 also explains the perceived potential competition theory. In this theory, the potential entrant is thought by industry participants to be an entrant and significantly constrains price. I understand that possibility but I have two concerns.

First, how would one know that the potential entrant significantly constrains price? Should the agencies be required to show this empirically? Or is it enough that some rival (that might fear the creation of an efficient rival) says so? If one is skeptical of self-interested testimony, as the 2023 Guidelines are in other places, why are they not concerned about that here?

Second, the clear insight of the Areeda-Turner test for predation is that having a standard for legality that depends on a rival's costs is not sensible since a firm knows only its own costs, not its rival's costs. That is why pricing "above cost" – above one's own cost – is no longer considered to be an anticompetitive act. But suppose that a firm has rejected entry and therefore acquisition is its only route to enter the

[18] *FTC v. Procter & Gamble Co.*, 386 U.S. 568, 577–578 (1967).

[19] Dillon (2011).

industry. Should the firm be deprived of that opportunity because its rivals testify that they believe (incorrectly) that the firm will enter on its own? Isn't that the same problem that Areeda-Turner pointed out with a predation standard based on rivals' costs? How is a firm supposed to know what its rivals are thinking?

Finally, again in the interests of balance, I would have liked to see some recognition that depriving a firm of the ability to purchase nascent firms could deprive those nascent firms of a way to cash out, thereby creating disincentives for them to enter. It is well known that exit choices influence entry rates. Will the agencies consider that? It is easy to see how in certain industries innovation is best done in small firms while the monetization of that innovation is best done by established firms. I see no recognition of that point in the 2023 Guidelines.

5 Guideline 5 Appears Hostile to Vertical Mergers

Guideline 5 is correct to explain that a vertical merger can harm competition. But as in the case of horizontal mergers, the Guideline's view seems to be a hostile one: Guideline 5 conveys an impression that the agencies believe that such mergers are frequently harmful and rarely beneficial. There is little if any explicit recognition, except perhaps in footnote 31, that a vertical merger involves a merger of complements in contrast to a horizontal merger that involves a merger of substitutes. By its very nature, a horizontal merger eliminates a rival and creates upward pricing pressure, all else equal. In contrast, by its very nature, a vertical merger creates a better alignment of incentives (e.g., the elimination of double marginalization) that should, all else equal, lead to downward, not upward, pricing pressure.

Of course, not all else is equal, especially in the case of a vertical merger. A vertical merger changes the incentive in setting the input price to (the now) downstream rivals and changes the incentive to set the downstream price of the merged firm. How all these forces play out depends in part on the diversion rates among the downstream products (and upstream products, if any). It also depends on how the pricing "game" changes. For example, if one thinks that, pre-merger, all prices are set in a sequential order involving Bertrand competition first at the upstream level and then at the downstream level, is it reasonable to continue that assumption post-merger when the upstream firm now controls both its upstream and downstream price?

My point is not to give vertical mergers a pass but instead that the Guidelines and enforcement based upon them should acknowledge the difference between horizontal and vertical mergers and the general lack of consensus in the economics profession about the likelihood of competitive harm from a vertical merger.[20]

But as in other parts of the 2023 Guidelines there seems to be a peculiar asymmetry in the treatment of evidence. Guideline 5 explains that there is evidence of a

[20] See, e.g., Carlton et al. (2019), Carlton (2020), Carlton and Israel (2021), Carlton et al. (2022), Crawford et al. (2018), Domnenko and Sibley (2023), and De Stefano and Salinger (2024). Carlton et al. (2022) contains a summary of the sparse empirical literature on vertical mergers. But see Loudermilk et al. (2023) and Salop (2018) for a different view.

possible harm if internal documents discuss limiting access post-merger. That seems right. But the Guideline goes on to suggest that it is not (equally?) probative if there are no such documents or apparently even documents indicating that there will be no such limitation of access. That does not seem balanced to me.

There is a discussion of contracts in footnote 31 as an alternative way to achieve any claimed benefits of a vertical merger that eliminates double marginalization. I will discuss contracts a bit more below; but here I ask why, if contracts can eliminate double marginalization, contracts have not already been written to do so?

But there is an even subtler point about contracts that the 2023 Guidelines have overlooked: Suppose absent the merger, the input monopolist uses non-linear pricing to write a contract with a downstream rival (with market power) to eliminate double marginalization AND as part of that contract also agrees to do this exclusively with this downstream firm. To all other downstream firms, the input price is a price above marginal cost. In return, the nonlinear pricing provides a payment to the input monopolist that splits the rents that arise downstream as a result of this favorable contract that harms the other downstream rivals. This is essentially an anti-competitive vertical merger that is achieved by contract.

Are the 2023 Guidelines claiming that this is better than the vertical merger? Or are they claiming that the agencies will investigate every vertical contract in every industry to make sure that there are no such payments?[21] If there are no transactions costs, then not only is the Guideline correct that the benefits of eliminating double marginalization by vertical integration can also be achieved by contract, but it also follows from that logic that the harmful effect on competition can be achieved by a vertical contract.

I understand that one response is that such a contract is illegal; but my point is that, given detection costs, harsh treatment of vertical mergers could lead to contracts that achieve similar ends but are hard to detect. Wouldn't it be better to have a vertical merger that is scrutinized and could involve a privately enforced contractual assurance of input supply at certain prices?

I fear that the agencies have not completely thought through the contract arguments in the 2023 Guidelines clearly. I will discuss this point further below.

Finally, as I discussed above, a vertical merger requires recalculating the altered incentives along a variety of dimensions. The upstream margin and downstream margins will change as a result of vertical integration and the resulting competition.[22] Guideline 5 says little explicitly about these margins as far as I can tell – other than the general statement that the competitive importance of the input will be evaluated.

[21] It was such concerns that motivated in part the Robinson-Patman Act, a law that is generally viewed as undesirable. Are the 2023 Guidelines suggesting that those views should be reexamined? If so, they should state this explicitly.

[22] The fact that vertical models are complicated means that, absent information on substitution among products and other information, one cannot isolate the effect of, say, elimination of double marginalization. In the *Illumina* case (*Illumina v. FTC*, No. 23–60,167 (5th Cir. 2023)), where I was a witness for the merging parties, I explained that, in the absence of a contract for the input, without a complete model one could do only illustrative calculations of, say, the benefit of the elimination of double marginalization; but, since no rival downstream products yet existed, there was no basis for me or the government's economist to estimate diversion ratios. I will return to the *Illumina* case briefly below.

For example, suppose a vertical merger involves an input monopolist (i.e., assume the input is sold by only one firm). If the downstream rivals are homogenous, and for some reason there is a margin downstream, then that merger can only benefit consumers[23]: Double marginalization is eliminated, and there is no harm to consumers if the downstream rivalry is eliminated. The overall margin goes down even if all downstream rivals are eliminated—and consumers benefit.

I would have liked to see some explicit recognition of this general point, even though the result need not always apply. For example, if goods are differentiated, then it might not apply.[24]

There is one additional point that is not mentioned in Guideline 5: Suppose that the vertical merger is announced and the enforcement agency is worried about complete foreclosure of downstream rivals by the input monopolist (the only supplier of the input). Also suppose that soon thereafter there are many new downstream rivals that announce that they have raised money to finance their downstream firms. Shouldn't that matter? The capital markets are telling us that they are not worried about complete foreclosure even though the enforcement agency is.

I would have liked to see at least some mention of this.

6 The 2023 Guidelines Pay No Attention to Contracts as a Way to Remove Harms to Competition from a Merger

I have already discussed the statements in the 2023 Guidelines that contracts might be able to achieve the benefits that are claimed by a proposed merger. Aside from these statements, the 2023 Guidelines are bereft of any discussion as to how contracts could eliminate concerns about harm to competition. It seems unbalanced to claim that contracts can be used to achieve the benefits of a merger, but not to recognize that contracts are capable of resolving the concerns of harm from a merger.

The point is most easily made in the context of a vertical merger: Suppose that an input monopolist acquires a downstream firm, which thereby raises the concern that the firm post-merger will foreclose other downstream rivals from access to the input or, alternatively, will raise the price of the input to the downstream rivals. To allay any such concerns, the firm offers a binding contract to any downstream rival that assures them access to the input at the pre-merger price. (To keep the example simple, assume that in the absence of the merger the input price would remain the same forever.)

Why doesn't that solve the concern with foreclosure? The downstream rivals have an enforceable contract whose breach would entail legal consequences. As long as the breach penalties are high enough, one should be able to create a self-enforcing

[23] A relevant issue is whether the assumption of an input monopolist is consistent with having large downstream margins. The discussion of critical loss earlier in the 2023 Guidelines emphasizes that the agencies will pay attention to margins to make sure that when an economic model such as critical loss is used to analyze a horizontal merger, the model is internally consistent with existing margins. That exact same logic should apply to vertical mergers – but it is not explicitly mentioned.

[24] See Carlton (2020, sec. 4).

contract that allays concerns about foreclosure.[25] Yet the 2023 Guidelines nowhere even suggest such a possibility, preferring in an early footnote (footnote 8) to state that remedies are not discussed.

A binding contract post-merger is an economic fact that one should take into account in assessing the effect of a proposed merger. Moreover, a binding contract among private parties is not a government-imposed remedy enforceable by the government. I understand that there can be a concern with government-enforced remedies, but a private contract does not raise those concerns – though it may raise concerns about private enforceability. It seems arbitrary to assert that such private contracts can never be properly enforced – especially if such contracts or similar ones already exist in the industry and especially if these types of contracts have resolved antitrust concerns in prior cases.[26]

7 Retrospective Studies

The 2023 Guidelines missed an opportunity to highlight the importance of retrospective studies. There are unavoidable tradeoffs in merger enforcement in deciding how aggressive or lax to be: Too aggressive a policy will scare off efficiency-enhancing mergers that would benefit consumers; and too lax a policy will harm consumers by harming competition. Balancing those tradeoffs appropriately can be aided greatly by examining how well past policy decisions have turned out. As I have discussed many times (see, e.g., Carlton (2009, 2022)), the best-situated economists to do those studies are the ones at the government agencies.

By a retrospective study, I mean much more than what is typically done where one examines whether prices went up or down after a merger. Notice that if the world is stable and only subject to random errors, then I would expect, absent other considerations, that half the time prices would go up and half the time down even if the merger had no adverse effect on competition; see Carlton (2009, 2022).

I would want to see a more in-depth study. For example, if a merger simulation model had been used, how well did those predictions turn out? If several such models had been used, which one did best? Was there information available during the merger investigation that would have allowed one to better predict the post-merger price increase if one did in fact occur? If the merging parties claimed that there would be efficiencies, were there? If the government blocks a merger because the

[25] Issues arising under contract law would have to be addressed to ensure that the contract is enforceable.

[26] For example, in the AT&T/Time Warner case (*United States v. AT&T, Inc.*, No. 18–5214 (D.C. Cir. 2018)), in which I served as an expert for the merging parties, Judge Leon noted that in a case that raised similar antitrust concerns (Comcast/NBCU) to those in the AT&T/Time Warner matter, the Department of Justice had argued that a remedy similar to the binding commitment that AT&T contractually obligated itself to in the AT&T/Time Warner matter had resolved the antitrust concerns of the Department of Justice. Judge Leon questioned why the contractual obligation in the AT&T/Time Warner case should not be expected to do the same. In the AT&T/Time Warner matter, the government unsuccessfully took the position, consistent with the 2023 Guidelines footnote 8 (which states that such "remedies" are beyond the scope of the Guidelines) that the legality of the merger should be addressed absent the "remedy." (Again, I defer to the legal scholars, but my reading is that the court again rejected that government position in *FTC v. Illumina*.).

acquisition is of a potential entrant, did that firm actually enter subsequently and become a significant rival?

Without such studies to assess past policy, I fear that antitrust policy will be set by the subjective preferences of the politicians and their appointees, and not by evidence. Such studies are needed if merger policy is to be evidence-based.

8 Praise

Although I have been critical of the 2023 Guidelines, it would be wrong to conclude that I reject much of the economic analysis presented in the 2023 Guidelines. The economics – primarily Sect. 4 – build upon prior Guidelines; and those Guidelines, though not perfect, did a good job. The economics in these Guidelines make several useful additions. I particularly liked some of the discussions about platform industries – especially the point that a merger that involves an intermediary that was a facilitator of competition among platforms could raise antitrust concerns, though I would have liked also to have seen some discussion of the possibility of free riding across platforms.

I also liked the point about bargaining that the 2023 Guidelines make – not just because I had made it too[27] but because it raises some deep questions about antitrust. In a bargaining environment, a merger can give a firm more bargaining power, and this can improve both efficiency and the merged firm's profits. But then that creates an incentive for the other side of the market to merge so as to offset this bargaining power and argue that its improved bargaining power will also increase efficiency. Pretty soon we have one firm on each side of the market.

The fundamental issue here is that the market forces lead to a structure that is as far from atomistic competition as one can get. It illustrates what Demsetz (1968) once stated: In the absence of transaction costs, there is no need for antitrust since the efficient solution will be reached. I don't believe that—neither did he—but it is a warning about the plausibility of such arguments. Moreover, the 2023 Guidelines, to their credit, address dynamic consequences, though predicting such consequences can be difficult.

Given the emphasis on labor markets in the Guidelines, I would hope that any merger that results in, say, a reduction in wages would pay attention to the long-run supply curve. I think especially of doctors' complaining about insurance companies getting larger through merger and then reducing reimbursement rates and wonder what effect that will have on the future supply of doctors.

My conclusion is that there is some good economics that has been added to the 2023 Guidelines but that the use of case citations and interpretations, together with the hostile tone in places to mergers and efficiencies, could have been omitted or at least could have appeared as a separate document. I expect that the next revision of the Guidelines will be sooner than the 13 years that have elapsed since the 2010 Guidelines.

[27] Carlton (2020).

Author contributions Dennis Carlton is the sole author.

Declarations

Competing interests I frequently work on matters before the enforcement agencies that are related to mergers and have worked for and against many of the largest firms that are involved in current litigation. I served as Deputy Assistant Attorney General in the Antitrust Division of the Department of Justice during 2006-2008 and was involved with the preparation of prior Merger Guidelines. When I mention a case in this article, I will indicate if I was involved in the case. My CV at Compass Lexecon lists the matters where my involvement is public. I thank Thomas Barnett, David Gelfand, Ken Heyer, Lewis Kaplow, Daniel O'Brien, Gregory Pelnar, Sam Peltzman, Steven Salop, Allan Shampine, Yoad Shefi, Ryan Shores, Theresa Sullivan, Larry White, and participants at my talks at the Federal Reserve Board and George Mason University for helpful comments.

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