German Law Journal (2024), pp. 1–31
doi:10.1017/glj.2024.44

CAMBRIDGE UNIVERSITY PRESS

ARTICLE

U.S. and EU Non-Horizontal Merger Guidelines: A Friendly Game of Leapfrog

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(Received 09 May 2023; accepted 05 August 2024)

Abstract

The accepted approach of competition law to non-horizontal mergers, largely based on the Chicago School of Antitrust Law and Economics paradigms, is criticized on both sides of the Atlantic as too lenient, disregarding developments of economic theory, and no longer adequate in the reality of the digital economy. Current economic research confirms the legitimacy of fears about the effects of non-horizontal concentrations that were raised before the Chicago School put them into doubt. The disbelief in the accuracy of the former US non-horizontal mergers policy resulted in the Federal Trade Commission and the Antitrust Division of the Department of Justice adopting new Vertical Merger Guidelines. The changes introduced were considered insufficient, which led to the unilateral repeal of the guidelines by the FTC and the start of work on new guidelines introducing a stricter approach. The new U.S. 2023 Merger Guidelines introduced far-reaching changes taking into account the modern views of economists and empirical research on vertical mergers. Comparatively, the EU Commission's Non–Horizontal Merger Guidelines still do not fully correspond to what empirical research and contemporary economic theories say about the possible effects of vertical mergers. Thus, the revision of the EU guidelines seems necessary.

Keywords: EU Competition Law; US Antitrust Law; Merger Control; Non-horizontal mergers

A. Introduction

With the ascendancy of the Chicago School of Antitrust Law and Economics, a tendency of lessening the intensity of enforcement of non-horizontal mergers has been visible on both sides of the Atlantic.[1] The well-established approach based on the Chicago School paradigms—focused on the effects that these transactions may have on prices and output— has been widely criticized as too lenient, disregarding the modern developments of economic theory, and no longer adequate to deal with new kinds of threats related to *inter alia* technological changes in the economy.[2]

[1]*See* Jonathan B. Baker, The Antitrust Paradigm: Restoring a Competitive Economy 44 (2019) (providing a reference to the United States' legal system's treatment of antitrust law).

[2]*Id.* at 2; Maurice Stucke & Allen Grunes, Big Data and Competition Policy 4–5 (2016); Steven C. Salop, *Invigorating Vertical Merger Enforcement*, 127 Yale L.J. 1962, 1966 (2018); Michael H. Riordan & Steven C. Salop, *Evaluating Vertical Mergers: A Post-Chicago Approach*, 63 Antitrust L.J. 513, 517 (1995); Michael B. Landau, *The Astounding Growth of "Big Tech" and the Lack of Enforcement of the Intellectual Property, Antitrust, and Contract Laws*, 30 Alb. L.J. Sci. & Tech. 1, 43–44 (2020); Charles A. Miller, *Big Data and the Non-Horizontal Merger Guidelines*, 107 Cal. L. Rev. 309, 318–20 (2019); Lina M. Khan, *Amazon's Antitrust Paradox*, 126 Yale L.J. 710, 731 (2017); Lina M. Khan & Sandeep Vaheesan, *Market Power and Inequality: The Antitrust Counterrevolution and Its Discontents*, 11 Harv. L. & Pol'y Rev. 235, 271 (2017).

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https://doi.org/10.1017/glj.2024.44 Published online by Cambridge University Press

It would be wrong however to analyze the current approach to vertical concentrations solely in the context of the development of the digital economy. The last few decades have been a period of both horizontal and non-horizontal consolidations of numerous industries.[3] It is hard to expect that this trend will change soon. On the contrary, it should be expected that the new economic reality emerging from the current geopolitical situation will only speed up this process. After the era in which the globalized economy relied on resource outsourcing, the global supply chains collapsed, first caused by the COVID-19 pandemic, and then by the Russian aggression on Ukraine.[4] The new *status quo* encourages producers to secure access to input to remain as resistant to rapid changes in the geopolitical situation as possible.[5] Tightening relationships with suppliers including through vertical integration seems to be the most effective answer to these problems.[6] Thus a new big wave of vertical acquisitions is yet to come.

Hence, it is even more important now than ever for Competition Authorities to have all the necessary tools enabling them to effectively distinguish between vertical concentrations that may harm the public interest and those that are neutral or may contribute to the achievement of net

[3]*See* Gábor Koltay & Szabolcs Lorincz, *Industry Concentration and Competition Policy*, *in* 2 European Commission: Competition Policy Brief (Nov. 2021). Koltay and Lorincz's studies prove increasing average industry concentration, and an increasing share of high concentration industries in four biggest EU countries and the UK in years 1999–2019. Moreover, the study confirms "increasing aggregate profit, with some industries—communication, finance, and transportation, as well as digitally intensive industries—particularly affected." *Id.* The U.S. is at least equally affected by the problem of the growing consolidation of industries. The study conducted by Thomas Philippon reveals that "the market shares of dominant firms are increasing in most U.S. industries." Thomas Philippon, *Causes, Consequences, And Policy Responses To Market Concentration, in* Maintaining The Strength Of American Capitalism 14, 29–30 (Melissa S. Kearney & Amy Ganz eds., 2019). This process has had serious detrimental effects on social welfare, since "[i]ncreased barriers to entry have resulted in lower investment, higher prices, and lower productivity growth." *Id.* at 30. "I estimate that the associated decline in competition has likely decreased aggregate labor income in the United States by more than $1 trillion between 2000 and 2019." *Id. See also* Diana L. Moss, *Merger Policy and Rising Concentration: An Active Agenda for Antitrust Enforcement*, 33 Antitrust 68, 69 (2018); Baker, *supra* note 1, at 20–22; Sean P. Sullivan, *Anticompetitive Entrenchment*, 68 U. Kan. L. Rev. 1133, 1137 (2020). The problem of overwhelming market concentration has been duly noticed by President Joe Biden who in his executive order held:

> Yet over the last several decades, as industries have consolidated, competition has weakened in too many markets, denying Americans the benefits of an open economy and widening racial, income, and wealth inequality .... Consolidation has increased the power of corporate employers, making it harder for workers to bargain for higher wages and better work conditions. Powerful companies require workers to sign non-compete agreements that restrict their ability to change jobs .... Consolidation in the agricultural industry is making it too hard for small family farms to survive. Farmers are squeezed between concentrated market power in the agricultural input industries—seed, fertilizer, feed, and equipment suppliers—and concentrated market power in the channels for selling agricultural products. As a result, farmers' share of the value of their agricultural products has decreased, and poultry farmers, hog farmers, cattle ranchers, and other agricultural workers struggle to retain autonomy and to make sustainable returns.

See Joe Biden, *Presidential Executive Order on Promoting Competition in the American Economy of July 09, 2021*, White House (July 9, 2021), https://www.whitehouse.gov/briefing-room/presidential-actions/2021/07/09/executive-order-on-promoting-competition-in-the-american-economy/

[4]*See* Benjamin Preston, *Global Chip Shortage Makes It Tough to Buy Certain Cars,* Consumer Reps. (May 6, 2021), https://www.consumerreports.org/buying-a-car/global-chip-shortage-makes-it-tough-to-buy-certain-cars-a8160576456/ (discussing one of the most striking examples, the semiconductor crisis which started in 2021 and caused shortages and delays in automobile production worldwide).

[5]*See* Daniel Gross, *Is Vertical Integration Making a Comeback?*, Strategy Bus. (Dec. 2, 2021), https://www.strategy-business.com/blog/Is-vertical-integration-making-a-comeback. *See also* Pierre-Nicolas Schwab, *The Return of Vertical Integration*, Into Minds (Jan. 31, 2022), https://www.intotheminds.com/blog/en/vertical-integration/.

[6]*See* Christian Schuh, Wolfgang Schnellbächer, Alenka Triplat and Daniel Weise, *The Semiconductor Crisis Should Change Your Long-Term Supply Chain Strategy*, Harv. Bus. Rev. (May 18, 2022), https://hbr.org/2022/05/the-semiconductor-crisis-should-change-your-long-term-supply-chain-strategy (advising that to prevent a similar future crisis, business leaders should "put suppliers at the core of the business" and car producers should work closer with their suppliers, the suppliers of their suppliers, and "every mission-critical company in their supply chain").

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economic efficiencies. Thus, a new approach based on modern knowledge and empirical research is needed.

The strong belief that the U.S. approach towards non-horizontal merger control has been a failure resulted in the adoption in 2020 by both American antitrust agencies of new Vertical Merger Guidelines ("U.S. 2020 VM Guidelines") that partially replaced the 1984 Merger Guidelines[7] based predominantly on the Chicago school paradigms. However, these changes were considered by Lina Khan's Federal Trade Commission ("FTC") as insufficient to effectively protect competition against threats from vertical mergers. The U.S. 2020 VM Guidelines were criticized primarily for their excessive belief in the procompetitive effects of vertical mergers and the failure to perceive the full spectrum of their possible detrimental consequences.[8] As a result, the FTC decided to temporarily withdraw the 2020 Vertical Merger Guidelines, pending the adoption of the new rules, "to prevent further industry or judicial reliance on certain flawed provisions."[9] The Department of Justice ("DOJ"), however, decided to continue to use the 2020 VM Guidelines, at the same time announcing they will work together with the FTC on updating the rules on vertical mergers.[10] Finally, following extensive public consultations, in December 2023 the Agencies published new Merger Guidelines ("U.S. 2023 Merger Guidelines").[11]

In light of these developments, are changes to the EU approach necessary? In particular, do the EU Non-horizontal Merger Guidelines ("EU NHM Guidelines")[12] require changes similar to those awaiting their American counterpart? It is clear that the EU approach towards vertical concentrations, as reflected in the EU NHM Guidelines, has long been stricter than the American. But do they provide proper tools for the assessment of vertical mergers? Are the theories of harm and efficiencies described in the guidelines consistent with the current state of economic research?

The U.S. 2023 Merger Guidelines represent an important step forward on the path to more effective control of anti-competitive concentrations, putting the U.S. system in the vanguard of competition law systems. The new standard for assessing vertical mergers provided in the guidelines is more stringent than the one provided for in the EU NHM Guidelines. Should then the EU join the U.S. in the antitrust leapfrog game in which the U.S. and the EU jump over their backs and swap places as non-horizontal mergers policy leaders?

In this Article, I have analyzed the evolution of the views of economics on the effects of vertical integration. I confronted them with the theories of harm and efficiencies stemming from vertical mergers as described in the U.S. 2020 VM Guidelines, the U.S. 2023 Merger Guidelines, and the EU NHM Guidelines. The latter have long been more in line with modern economic theories than their American counterpart. Now, after the introduction of the U.S. 2023 Merger Guidelines, the situation has changed. EU guidelines seem to overestimate the positive nature of vertical concentrations and underestimate their potential negative effects. Thus, the guidelines require modifications to describe theories of harm, and changes in the rhetoric used by the EU Commission to describe the possible outcomes of non-horizontal concentrations.

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[7]*See* U.S. Dep't of Just. & Fed. Trade Comm'n, 1984 Merger Guidelines (1984).

[8]*Statement of Chair Lina M. Khan, Commissioner Rohit Chopra, and Commissioner Rebecca Kelly Slaughter on the Withdrawal of the Vertical Merger Guidelines of September 15, 2021 (Commission File No. P810034)*, 2 FTC. *See also* James Keyte, *The Draft Vertical Merger Guidelines: A Modern Approach, But Gaps and Questions Remain*, 34 Antitrust 5, 6–7 (2020).

[9]*Id. See also Statement of FTC Chair Lina Khan and Antitrust Division Acting Assistant Attorney General Richard A. Powers on Competition Executive Order's Call to Consider Revisions to Merger Guidelines* (July 9, 2021), https://www.ftc.gov/news-events/press-releases/2021/07/statement-ftc-chair-lina-khan-antitrust-division-actingassistant.

[10]*See* Press Release, Dep't Just., Just. Dep't Issues Statement on the Vertical Merger Guidelines (Sep. 15, 2021), https://www.justice.gov/opa/pr/justice-department-issues-statement-vertical-merger-guidelines.

[11]*See* U.S. Dep't of Just. & Fed. Trade Comm'n, Merger Guidelines (2023) [hereinafter U.S. 2023 Merger Guidelines].

[12]The Commission Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings, 2018 O.J. (C 265) 6, 6–25.

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Below, the results of the analysis of the evolution of the views of economics on the effects of vertical integration are presented. The results of this analysis were confronted with the theories of harm and efficiencies resulting from vertical mergers as applied by the U.S. federal courts and developed in the U.S. 2020 VM Guidelines and subsequently U.S. 2023 Merger Guidelines. This made it possible to show the dynamics, origins, and basic assumptions of changes in the standard for assessing vertical concentrations in the U.S. Finally, the theories of harm and efficiencies described in the EU NHM Guidelines were analyzed. Following their comparison with the U.S. 2023 Merger Guidelines, they were confronted with the current economic concepts of the competitive effects of vertical mergers.

B. The Competitive Effects of Vertical Integration

I. Early Concepts

The field of economics did not pay much attention to vertical integration until the end of the 1910s. In the works of classical economists, there are only a few references to this area, usually in a general context of the economy of scope and specialization.[13]

Vertical integration was the subject of a broader reflection by Alfred Marshall.[14] This author associated vertical integrations' intensification with the diversification of the goods produced in a given market, as well as with a firm's concerns for quality and production costs. According to Marshall's views, the progressive differentiation of goods produced by a company favors vertical integration, as it requires the supply of more specialized inputs.[15]

Joe Bain, the father of industrial organization economics, referred to both the reasons and the effects of vertical integration.[16] In addition to the common rationale for both vertical and horizontal integration, such as free funds for investments and managerial personal motivations, Bain pointed out that diversification mergers—vertical or conglomerate—may be motivated by the search for the most profitable investment.[17] Vertical integration may as well be a part of "predatory or exclusionary tactics," focused on the monopolization of raw material supplies, or distributive outlets to restrict access of smaller and usually non-integrated competitors to indispensable resources or distribution channels.[18]

Bain considered vertical integration to be an imminent source of implicitly exclusionary effects. According to Bain, these effects were obvious—vertically integrated companies have no incentives to purchase from or deliver inputs to non-integrated companies, reducing their welfare. At the same time, efficiencies resulting from vertical integration may allow companies to sell at a lower price than that offered by a non-integrated competitor, which may lead to a market exit of the latter.[19] Among other possible adverse effects of vertical mergers, Joe Bain mentioned: (1) The price squeeze, (2) the semi-squeeze, and (3) the unequal supplying of nonintegrated competitors.[20]

[13]*See* Herbert Hovenkamp, *The Law of Vertical Integration and the Business Firm: 1880-1960*, 95 Iowa L. Rev. 863, 870–71 (2010) (according to Hovenkamp, "most of the classicists simply assumed that the firm procured some of its needs on the market and did other things for itself depending on convenience"). Adam Smith's observations regarding interdependence between the scope of a market and the division of labor has been translated by George J. Stigler into observations of assumptions of his vertical integration theories pursuant to which the larger the market, the greater the economy of specialization and scale. George J. Stigler, *The Division of Labor Is Limited by the Extent of the Market*, 59 J. Pol. Econ. 185, 189 (1951) (observing that "vertical disintegration is the typical development in growing industries, vertical integration in declining industries").

[14]Alfred Marshall, Industry and Trade: A Study of Industrial Technique and Business Organization; And of Their Influences on the Condition of Various Classes and Nations 146–58 (1st ed. 1919).

[15]*See* Hovenkamp, *supra* note 13, at 872. *See also* Marshall, *supra* note 14, at 152.

[16]Joe S. Bain & P. David Quails, Industrial Organization: A Treatise 168 (1987).

[17]*Id.*

[18]*Id.* at 260.

[19]*Id.* at 484–85.

[20]*Id.* at 261–63. Bain differentiated between the price squeeze and the semi-squeeze. The former refers to the situation in which a vertically integrated producer of a raw material, and a finished good made from it, increases the price of the raw material in sales to a nonintegrated producer to the level of the finished goods prices, thus squeezing a margin collected by it to

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Moreover, according to Bain, vertical and conglomerate mergers inevitably lead to an undesirable concentration of companies' sizes and of the economy as a whole.[21]

This does not mean, however, that Bain believed that vertical integration always had net anticompetitive effects, let alone that it should be presumed illegal. On the contrary, such a prohibition in Bain's view should only concern integration, the effect of which could be "to unreasonably restrict the opportunities of competitors to market their product."[22]

In sum, Bain showed serious distrust toward vertical integration, which in his view could lead to two types of harm: Foreclosure and an unfavorable change in the market structure. At the same time, Bain recognized that the intensity of these effects increased proportionally to the degree of market concentration, either at the upstream or downstream level. Although Bain recognized certain efficiencies of vertical integration, including primarily cost reductions, he strongly emphasized its anti-competitive motivations, at least when it took place in concentrated markets.

The skepticism towards vertical mergers expressed by representatives of traditional industrial organization economics influenced the later approach towards vertical mergers in the 1950s and 1960s. For instance, in their treatise published in 1965, Carl Kaysen and Donald F. Turner proposed the establishment of a *prima facie* illegality criterion for "an acquisition of a relatively substantial customer or supplier by a firm with 20 percent of its primary market . . . ."[23]

Representatives of institutional economics devoted much attention to vertical integration. They usually referred to it in the context of the relationship between ownership and management in a company. As it could be deduced from Adolf Berle's and Gardiner Means' theory, vertical integration can be motivated by managers' tendency to increase their profits and broaden the scope of their power.[24] From this perspective, vertical integration seems to be considered both an undesirable, indirect consequence of the separation of ownership and control in a firm and also a factor conducive to the intensification of the process of such separation. It was understood that if, as a result of a merger, the ownership management was replaced by a professional team, it normally led to increased agency costs. Mergers were thus considered to contribute to the unwelcome separation of ownership and control, as well as being deemed a source of inefficiency.[25]

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such an extent that it makes no profits or suffers losses. The semi-squeeze covers a similar situation, however in this case an integrated company sells raw materials with a margin sufficient for a nonintegrated competitor to make some profits, but still at prices excessive and high enough to make it difficult for them to compete effectively in the market for the finished good. *Id.*

[21] *Id.* at 168.

[22] *Id.* at 486. According to Bain, this should apply to vertical integration fulfilling three criteria:

> (1) [T]hat vertical integration with implicitly restraining influences is likely to be found illegal only in cases where in conjoined with predominant horizontal market control by a monopolist or joint monopolists in one or more of the vertical sequences of markets involved, this being evidence that the integration may have played some role in the creation or maintenance of predominant horizontal occupancy; (2) that the vertical integration, to be illegal, must be in some degree crucial to the maintenance of the predominant occupancy, in the sense that its elimination might undermine the basis of such occupancy; and (3) that the vertical integration, if illegal, has been exploited at least by normal and prudent business practices having exclusionary effect and inferred purpose, though not necessarily by express Section 1 offenses.

Id.

[23] Carl Kaysen & Donald F. Turner, Antitrust Policy: An Economic and Legal Analysis 133 (1965). According to Kaysen and Turner, the correct approach to enforcement of vertical mergers should be based on the government proving existing market power and a probability that it would result in its extension into the new field or enhanced by the merger. *Id.* In proving this, the key importance should be given to structural rather than behavioral evidence, which was a consequence of focusing the merger analysis on its future, not past effects. *Id.*

[24] Adolf A. Berle & Gardiner C. Means, The Modern Corporation and Private Property 308 (Rev. ed. 1968).

[25] *See id.* Berle and Means were skeptical about the effective operation of the competition mechanism in a market dominated by large corporations, as opposed to a market involving small, individually controlled operators. As they argued:

> Finally, when Adam Smith championed competition as the great regulator of industry, he had in mind units so small that fixed capital and overhead costs played a role so insignificant that costs were in large measure

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Ronald H. Coase saw the reasons behind vertical integration in the effectiveness resulting from the avoidance of transaction costs that were normally associated with repetitive contracts with an external contractor.[26] He compared vertical integration to a long–term contract created by a firm with an employee. In this approach, vertical integration takes place when its costs are lower than the costs of obtaining similar effects on the market.[27]

Coase's theory was developed by Oliver Williamson[28] and then by Benjamin Klein, Robert G. Crawford, and Armen A. Alchian, who added that contractual relations between non-integrated companies may be opportunistic. The theorists observed this phenomenon is particularly visible if non-integrated companies are concerned with goods tailored to the buyer's needs and primarily contract on an incomplete basis.[29] In such a situation, a party to an agreement may try to use ambiguities in a contract to their advantage, resulting in inefficiency. At the same time, a change of contractor or contract litigation may appear costly for the remaining party.[30]

Subsequent studies on the theory of property rights and the impact of vertical integration on transaction costs led Sanford J. Grossman and Oliver D. Hart to formulate their thesis that vertical integration leads to the adoption of a specific model of allocation of residual rights between the parties. However, that allocation does not eliminate incentives for opportunistic and distortionary behavior but merely shifts the rights between the parties.[31] As a result of integration, purchasing residual rights by one party and subsequent loss of those rights by another inevitably creates distortions.[32] Economic models developed by Oliver D. Hart and Jean Tirole are important contributions to the understanding of societal gains and societal losses resulting from vertical integration. The societal losses include: (i) Price increases resulting from ex-post monopolization[33]; (ii) exits from the market of upstream or downstream competitors of the merged firms, or both of them[34]; and (iii) incentives and legal costs.

> determinate and so numerous that no single unit held an important position in the market. Today competition in markets dominated by a few great enterprises has come to be more often either cut-throat and destructive or so inactive as to make monopoly or duopoly conditions prevail. Competition between a small number of units each involving an organization so complex that costs have become indeterminate does not satisfy the condition assumed by earlier economists, nor does it appear likely to be effective a regulator of industry and of profits as they had assumed.

Id.

[26]*See* Ronald H. Coase, *The Nature of the Firm*, 4 Economica 386, 394–95 (1937). *See also* Patrick Bolton & David S. Scharfstein, *Corporate Finance, the Theory of the Firm, and Organizations*, 12 J. Econ. Perspectives 95, 97 (1998); Timothy J. Brennan, *Vertical Mergers, the Coase Theorem, and the Burden of Proof*, 16 J. Comp. L. & Econ. 488, 490 (2019).

[27]As Coase pointed out, enlargement of the firm, including by the vertical integration, takes place as "the costs of organizing certain transactions within the firm may be greater than the costs of carrying out the exchange transactions in the open market." Coase, *supra* note 26, at 396. *See also* Sanford J. Grossman & Oliver D. Hart, *The Costs and Benefits of Ownership: A Theory of Vertical and Lateral Integration*, 94 J. Pol. Econ. 691, 692 (1986).

[28]*See* Oliver E. Williamson, Markets and Hierarchies: Analysis and Antitrust Implications: A Study in the Economics of Internal Organization 26–30 (1975). *See generally* Oliver E. Williamson, The Economic Institutions of Capitalism (1985).

[29]Robert G. Crawford, Benjamin Klein and Armen A. Alchian, *Vertical Integration, Appropriable Rents, and the Competitive Contracting Process*, 21 J.L. & Econ 297, 302–07 (1978).

[30]*See id.* at 307. As Bolton and Scharfstein pointed out, "integration into a single corporation should occur when renegotiation costs are high and when important relationship-specific investments exist." Bolton & Scharfstein, *supra* note 26, at 98. *See also* Grossman & Hart, *supra* note 27, at 692.

[31]*See* Grossman & Hart, *supra* note 27, at 716. *See also* Oliver Hart & Jean Tirole, *Vertical Integration and Market Foreclosure*, 21 Brookings Papers on Econ. Activity 205, 206 (1990); Bolton & Scharfstein, *supra* note 26, at 112 (explaining that full understanding of the effects of integration requires studies on the effectiveness of the bargaining process among divisional managers and headquarters such as the efficiency of the firm's decisionmaking processes).

[32]Grossman & Hart, *supra* note 27, at 716.

[33]Hart & Tirole, *supra* note 31, at 211. This situation may take place when a relatively efficient upstream firm takes control over a downstream player in order to restrict output on the downstream market.

[34]This may appear in all three variants developed by Hart and Tirole. The first occurs when a relatively efficient upstream firm takes control over a downstream player in order to restrict output on the downstream market. *Id.* at 208. The second

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These societal losses may be compensated by the potential gains from the mergers. One example could be savings in investment costs, which may offset the market exit of a downstream or upstream competitor. This could be "beneficial to the extent that it leads to a reduction in rent-seeking behavior."[35] Another example could be pure efficiency benefits, such as ex-ante investments—this refers to mergers motivated by a necessity to encourage investments to decrease holdup problems.[36]

According to Hart and Tirole, it would be difficult to set clear-cut guides for the antitrust treatment of vertical integration.[37] However, as they pointed out, negative effects on competition from vertical mergers take place more often when merging firms are more efficient or larger than their competitors.[38] Moreover, as Hart and Tirole held, antitrust scrutiny should focus on mergers that significantly harm competitors, which is to say, those between firms that have well-developed trade with third parties before the merger.[39]

II. The Chicago School of Law and Economics

Vertical and conglomerate integration was one of the central areas of the Chicago School's interest. One of its precursors, George J. Stigler wrote in 1951 about vertical and conglomerate integration causes and effects in the broader context of research on the development of the famous Adam Smith theorem: "[T]he division of labor is limited by the extent of the market."[40] Stigler however did not aspire to create a comprehensive theory of vertical integration. Instead, he pointed to the selected factors that may favor it and to its specific results. Quite surprisingly, this Chicago School pioneer seemed to be suspicious about the effects these practices could have on competition.[41]

Developing the view of Adam Smith, Stigler argued that the intensity of vertical integration processes depends on the degree of development of a given industry. Young industries as new players in a firmament of economic systems need specialized products or services which are scarcely available on the open market, which tends to encourage consumers to switch to their product. This may require starting the production of necessary equipment and raw materials as well as forming an independent distribution and promotion of a new product. Along with the development of the industry, specialized suppliers of raw materials, equipment, and services will appear. Accordingly, it may be profitable for a producer to entrust these activities to specialized firms. As industry declines, the number of complementary industries drops as well. This drop requires the producer to expand the scope of its activities to cover these complementary products and services, which cannot be effectively contracted on the open market.[42]

Stigler associated another rationale for vertical integration with the failure of price systems resulting from a monopoly—including cartels—or public regulation. In such a situation,

occurs when needs are scarce, which is to say when equally efficient upstream and downstream companies bargain over the gains from trade and as a result only an upstream firm gains adequate share of this gains. *Id.* at 210. In such circumstances, an upstream player may want to take control over a downstream firm to ensure that the latter purchases supplies from the former rather than from the others. *Id.* at 210. The third variant occurs when supplies are scarce, which is to say, when upstream and downstream firms negotiate terms of trade on a market in which upstream firms are "are capacity-constrained relative to downstream firms' needs." *Id.* 210. In these circumstances, a downstream firm may have the incentive to merge as to safeguard the supplies of scarce resource from an upstream party. *Id.* at 211.

[35]*Id* at 211.

[36]Hart & Tirole, *supra* note 31, at 211–12.

[37]Hart & Tirole, *supra* note 31, at 213.

[38]*Id.*

[39]*Id.*

[40]George J. Stigler, *The Division of Labor is Limited by the Extent of the Market*, 59 J. Pol. Econ., 185–93 (1951).

[41]*Id.* at 191 (noting that "as soon as one tries to classify the variegated details of production, one finds how artificial and arbitrary 'vertical' relationships are").

[42]*Id.* at 189–90.

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producers will look for the possibility of cheaper supplies, cheaper services, or both, including through vertical integration. According to Stigler, a monopoly may be a stimulus favoring vertical integration, as it could facilitate the use of predatory pricing by the dominant company. Vertically integrated monopolists may cross-subsidize the prices of goods offered in markets with a higher level of competition by charging supracompetitive prices for products sold in monopolized markets.[43] Vertical integration may also increase market entry barriers by "increasing the capital and knowledge necessary to conduct several types of operation rather than depending on rivals for supplies or markets."[44]

Other representatives of the Chicago School highlighted the positive effects of vertical and conglomerate mergers, usually downplaying negative impact of mergers on competition. Their main argument supporting the thesis of the efficiency of vertical mergers refers to the elimination of double marginalization ("EDM") which has been considered vertical mergers' inevitable consequence.[45] According to this concept, a vertically integrated producer sells goods to its downstream subsidiary at a price equal to marginal cost, which leads to the latter lowering the price of the final product. This means customers benefit from lower prices and higher output. EDM was first developed by Joseph J. Spengler in 1950. Spengler considered vertical integration to be a remedy for "the rent–like 'monopolistic' surcharges being imposed by sellers situated in earlier stages of production."[46]

Robert Bork devoted significant attention to non-horizontal mergers in his *Antitrust Paradox*, a bible-like text of the then-emerging and powerful current.[47] Bork attacked the prevailing views on the effects and enforcement of vertical and conglomerate mergers, recognizing vertical integration as nothing more than one of the ways of organizing "the cooperation of two or more persons engaged in a productive or distributive activity."[48]

According to Bork, the foreclosure theory as applied by the U.S. Supreme Court in the *Brown Shoe*[49] case was "completely improper."[50] In the *Brown Shoe* case—which provided the foundations for the assessment of vertical mergers—the Supreme Court held that the acquisition by the fourth largest shoe manufacturer, Brown Shoe, of the largest U.S. family–style shoe store chain, G.R. Kinney Co., could substantially lessen competition, thus infringing upon § 7 of the Clayton Act. Despite the fact that Brown Shoe's share of U.S. shoe production was only 4% and the fact G.R. Kenney's share of shoe sales in the U.S. amounted to only 1.2%, the merger was considered anticompetitive. This holding was mainly due to the potential input and customer foreclosure effects depriving Brown Shoe's "rivals of a fair opportunity to compete."[51]

According to Bork, taking control over a retailer and forcing it to sell only goods provided by the purchaser cannot be profitable. As Bork argued, in such a situation, even if a supplier has

[43]*Id.* at 190–91.

[44]*Id.* at 190.

[45]*See* Richard A. Posner, Antitrust Law 200–01, 228 (2nd ed. 2001) [hereinafter Posner, Antitrust Law II]. *See also* Géarard Gaudet & Ngo Van Long, *Vertical Integration, Foreclosure, and Profits in the Presence of Double Marginalization*, 5 J. Econ. & Mgmt. Strategy 409, 409 (1996).

[46]Joseph J. Spengler, *Vertical Integration and Antitrust Policy*, 58 J. Pol. Econ. 347, 351 (1950) ("Vertical integration serves, therefore, to make price structures and factor allocation more ideal than they otherwise would be in an imperfectly competitive world."). For an illustrative explanation of the elimination of double marginalization theory, see generally John Kwoka & Margaret Slade, *Second Thoughts on Double Marginalization*, 34 Antitrust 51 (2020).

[47]Robert H. Bork, Antitrust Paradox: A Policy at War with Itself 225–45 (1st ed. 1978). *See generally* Robert H. Bork, *Vertical Integration and Competitive Processes*, *in* Public Policy Toward Mergers 139 (John Fred Weston & Sam Peltzman eds., 1969).

[48]Bork, Antitrust Paradox, *supra* note 47, at 227 (pointing out at the same time a firm is in the best position to properly assess the optimal way in which it organizes such cooperation). *See also* John S. McGee & Lowell R. Bassett, *Vertical Integration Revisited*, 19 J.L. & Econ. 17, 17–18 (1976).

[49]Brown Shoe Co. v. United States, 370 U.S. 294, 332–34 (1962) (applying the foreclosure theory).

[50]Bork, Antitrust Paradox, *supra* note 47, at 227.

[51]*Brown Shoe Co.*, 370 U.S. at 324.

https://doi.org/10.1017/glj.2024.44 Published online by Cambridge University Press

doubled its market share, it cannot make a profit because, in a competitive environment, it would not be able to increase the price above the level of its marginal costs. At the same time, the purchased retailer would suffer losses due to its resignation from the most efficient distribution pattern that had been applied before the merger.[52] Bringing this "imperialistic dream" to life might also entail increased management costs.[53]

Another one of Bork's arguments relied on his theory of a "single monopoly profit."[54] Bork argued that a vertically integrated company would not sell a product to a controlled retailer for a price lower than the one charged to third parties. Otherwise, it would bear the cost of the forgone opportunity, which could not be compensated by higher retail prices unless the firm was a natural monopolist. Consequently, this would result in increased output at higher costs.[55]

Finally, Bork held that vertical mergers normally led to numerous efficiencies, including cutting sales and distribution costs, thereby facilitating the flow of information and creating economies of scale in management. In his opinion, vertical mergers were generally not different from internal growth. The only difference was that in a certain market situation, a vertical merger or internal growth is a more effective option.[56]

Richard Posner also took the position that there are essentially positive effects of vertical integration. Posner referred to arguments that explained how if a merger resulted in serious upstream or downstream foreclosure, new entrants may have to enter both the upstream and downstream markets. Expressing his usual skepticism about the relevance of entry barriers, he claimed that vertical integration may delay—though not prevent—market entry. According to Posner, when a monopoly producer purchases the distributors' outlets, the monopoly price may increase, and the costs of market entry may also rise. However, this generates significant costs, resulting from (1) abandoning the benefits of giving some excess distributive capacity to a competitor; (2) possible diseconomies of vertical integration; and[57] (3) the creation of incentives to start distribution outlets by third parties.[58] These costs may effectively discourage monopolizing distribution.[59] Similarly, purchasing all distribution outlets would not be profitable for a producer active in an oligopolistic market. Such a merger would result in gaining control over an excessive distributive capacity and a significant increase in the producer's distribution costs. Also, a competitor would invest in his distribution network or contract with a new entrant on a distribution level.[60]

[52]*See* BORK, ANTITRUST PARADOX, *supra* note 47, at 227. *See also* RICHARD A. POSNER, ANTITRUST LAW: AN ECONOMIC PERSPECTIVE 196 (1st ed. 1976) [hereinafter POSNER, ANTITRUST LAW I].

[53]BORK, ANTITRUST PARADOX, *supra* note 47, at 229.

[54]*Id. See also* Robert H. Bork, *Vertical Integration and the Sherman Act: The Legal History of an Economic Misconception*, 22 U. CHI. L. REV. 157, 195–97 (1954); POSNER, ANTITRUST LAW I, *supra* note 52, at 197.

[55]As Posner pointed out, it makes no sense for a monopoly producer to take over distribution in order to earn monopoly profits at the distribution as well as the manufacturing level. The product and its distribution are complements, and an increase in the price of distribution will reduce the demand for the product. Richard A. Posner, *The Chicago School of Antitrust Analysis*, 127 U. PA. L. REV. 925, 927 (1979). *See also* Bork, *Vertical Integration and Competitive Processes*, *supra* note 47, at 169.

[56]POSNER, ANTITRUST LAW I, *supra* note 52, at 196 (claiming that "the same effect (as in the case of vertical merger – Ł.G.) can be achieved without any acquisition, by the firm's opening a new outlet, or a new source of supply, and channeling all sales (or all purchases) through the new division").

[57]*Id.* at 199 ("Integration for purposes of exclusion implies that there are no economies of integration (if there were such economies, that would be an independent and socially acceptable reason for integration). And if there are no economies of integration there are probably diseconomies.").

[58]In the new edition of his treatise Posner adds that delays in new entries may make a market entry more attractive, "because now they can anticipate a longer period before any profits that they obtain in the market are eliminated by the competition of still newer entrants." POSNER, ANTITRUST LAW II, *supra* note 45, at 226.

[59]*See* Posner, *The Chicago School of Antitrust Analysis*, *supra* note 55, at 936 (referring to the impact of vertical mergers on creation of barriers to entry, Posner held that "the steps in this analysis are illogical, however, and evidence of monopolization by such means scant or nonexistent").

[60]POSNER, ANTITRUST LAW I, *supra* note 52, at 199.

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According to Posner, even a merger between two firms occupying a monopolistic position in the subsequent chains of product distribution should not be prohibited.[61] Such mergers, by lowering costs of distribution, may result in a decrease in the price of the final product, and thus its output would increase.

The only type of vertical merger that Posner considered potentially harmful was the takeover of a final product manufacturer by a monopoly producer of raw materials, used in variable proportions with other inputs, to produce the final product. Such concentrations should, according to Posner, be treated as horizontal. However, even in such a case, the mergers' assessment should depend on the specific circumstances of the case, and should not lead to an automatic prohibition.[62]

III. Chicago School Critique and Current Discussion on Vertical Mergers

From the outset, the ideas of the Chicago School have been criticized, mainly by neo-Chicago economists.[63] Neo-Chicagoan research called into question the basic Chicagoan assumptions related to the effects of vertical mergers on the competition.

Neo-Chicagoan research served as a foundation for Neo-Brandeisian ideas.[64] Neo-Brandeisians see the excessively liberal approach of American antitrust law's treatment of non-horizontal mergers inspired by the Chicago school as one of the reasons for the unprecedented and detrimental growth of the power of big-tech companies.[65]

In the opinion of Chicago School critics, expressed mainly by Steven C. Salop, the concepts of the Chicago School have been based on oversimplified economic models disregarding many important market circumstances.[66] While it is true that some vertical mergers may bring no negative effects, this does not account for mergers taking place in markets characterized by imperfect competition.[67] Salop has challenged the Chicago School's views regarding the impact of vertical integration on competition.[68] According to Salop, contrary to Bork's claims, foreclosure is a real and not merely illusory effect of a merger.

It is worth noting that market foreclosure has long been understood as the primary antitrust concern resulting from vertical integration. A vertical merger may result in input foreclosure when, following a merger with a downstream company, an upstream firm—like a manufacturer—disadvantages the former competitors by limiting or denying input. This type of action can take various forms, including raising the prices of products, decreasing product quality, raising transaction costs, or expressly refusing to supply competitors. This in turn may result in a price increase of a downstream product due to the lowering of competitive constraints. More pressure is then exerted on a downstream party, thus strengthening the upstream firm's market power.

[61]Posner, Antitrust Law II, *supra* note 45, at 228.

[62]*Id.* at 200–01.

[63]*See generally* Jonathan B. Baker, *Exclusion as a Core Competition Concern*, 78 Antitrust L.J. 527 (2013); Janusz A. Ordover, Garth Saloner and Steven C. Salop, *Equilibrium Vertical Foreclosure*, 80 Am. Econ. Rev. 127 (1990); Patrick Rey & Jean Tirole, *A Primer on Foreclosure*, *in* Handbook of Industrial Organization 2145 (Mark Armstrong & Robert H. Porter eds., 2007); Michael H. Riordan, *Competitive Effects of Vertical Integration*, *in* Handbook of Antitrust Economics 145 (Paolo Buccirossi ed., 2008); Michael H. Riordan & Steven C. Salop, *Evaluating Vertical Mergers: A Post-Chicago Approach*, 63 Antitrust L.J. 513 (1995); Michael Salinger, *Vertical Mergers and Market Foreclosure*, 103 Q.J. Econ. 345 (1988); David T. Scheffman & Richard S. Higgins, *Vertical Mergers: Theory and Policy*, 12 Geo. Mason L. Rev. 967 (2004).

[64]Richard J. Gilbert & A. Douglas Melamed, *Innovation: A Bridge to the New Brandeisians?*, Competition Pol'y Int'l (Feb. 21, 2022), https://www.competitionpolicyinternational.com/innovation-a-bridge-to-the-new-brandeisians/#_ftnref6.

[65]*See* Khan, *Amazon's Antitrust Paradox*, *supra* note 2, at 731–36; Tim Wu, The Master Switch: The Rise and Fall of Information Empires 307 (2011).

[66]*See, e.g.*, Riordan & Salop, *Evaluating Vertical Mergers*, *supra* note 2, at 517.

[67]*See* Salop, *Invigorating Vertical Merger Enforcement*, *supra* note 2, at 1966.

[68]*Id.* at 1967–68.

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Foreclosure may equally refer to customers. In this situation, a supplier takes control over a producer, or a distributor, and limits or deprives its competitors of access to a market by eliminating a potential buyer.[69] This may result in the strengthening of the market power of an upstream firm.

As Salop rightly argues, the well-established horizontal merger theory for companies selling differentiated products is also applicable to a vertical merger taking place in similar market structures.[70] Under this theory, companies selling differentiated products may decrease competition by enabling a merged firm to achieve higher profits through raising a price unilaterally. In such a situation, part of the losses resulting from an increase in price could be compensated for by redirecting sales to the products offered by the other party to the merger. Similar price pressure is an intrinsic consequence of a vertical merger in a market where differentiated products are produced. Here, an upstream party to such a merger has an analogical incentive to engage in input foreclosure by raising the input price. This incentive may then be outweighed by upstream or downstream competition from an expected market entry, or by efficiencies, including the elimination of double marginalization.[71]

According to Salop, following the acquisition of a large distributor, an oligopolistic upstream company offering diversified products would limit its sales to competitors of the downstream parties to the merger. The upstream company would accomplish this by increasing prices or simply refusing to sell to the downstream company. This may induce rivals of an upstream company to similarly raise the price of their products, either due to unilateral or coordinated conduct. The result of either would be an increase in the market power of the merged company in one or both markets.[72]

It is possible, however, that a vertical merger will not result in foreclosure, but only when the merger is pursued in a non-concentrated market. This does not mean that foreclosure may never arise in such a market. This may be the case if a concentration would lead to the elimination of a maverick firm, having relatively small market share but exerting competitive pressures before the merger on downstream—input foreclosure—or upstream competitors—customers foreclosure.[73]

The negative effects of market foreclosure may increase as well because of a unique position of a remaining competitor, illustratively denominated by Krattenmaker and Salop as "Frankenstein monster."[74] This notion refers to the last independent supplier remaining on the market after a vertical merger. Such a "monster" may monopolize the upstream market, thus raising the costs of downstream competitors of a vertically integrated company. Similarly, by reducing the number of

[69]*See* Thomas G. Krattenmaker & Steven C. Salop, *Anticompetitive Exclusion: Raising Rivals' Costs to Achieve Power over Price*, 96 YALE L.J. 209, 218 (1986) (referring jointly to the effects of vertical exclusivity agreements and vertical mergers). *See generally* Jonathan M. Jacobson, *Vertical Mergers: Is It Time to Move the Ball?*, 33 ANTITRUST 6 (2019).

[70]This theory was extensively described in Section 6.1. of the 2010 U.S. Horizontal Merger Guidelines:

> The extent of direct competition between the products sold by the merging parties is central to the evaluation of unilateral price effects. Unilateral price effects are greater, the more the buyers of products sold by one merging firm consider products sold by the other merging firm to be their next choice.

U.S. DEP'T OF JUST. & FED. TRADE COMM'N, HORIZONTAL MERGER GUIDELINES 20 (2010) [hereinafter U.S. 2010 HORIZONTAL MERGER GUIDELINES].

[71]*See* Salop, *Invigorating Vertical Merger Enforcement*, *supra* note 2, at 1973. *See also* Serge Moresi & Steven C. Salop, *vGUPPI: Scoring Unilateral Pricing Incentives in Vertical Mergers*, 79 ANTITRUST L.J. 185, 186 (2013).

[72]*See* Salop, *Invigorating Vertical Merger Enforcement*, *supra* note 2, at 1973.

[73]Accordingly, as held by Salop:

> "the agencies might consider a possible near-safe harbor if both markets are unconcentrated, and if concentration also would be low for a modified measure of concentration, where the merging firms are excluded from the concentration calculation. The latter calculation is needed to take into account the incentives of nonmerging firms to respond to foreclosure by raising their own prices"

Id. at 1989–90. *See generally* STEVEN C. SALOP & DANIEL P. CULLEY, VERTICAL MERGERS ENFORCEMENT ACTIONS: 1994-2016 (2017).

[74]Krattenmaker & Salop, *supra* note 69, at 240.

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independent suppliers, a vertical merger may facilitate collusion between the remaining suppliers, thereby leading to coordinated effects.[75]

Chiara Fumagalli's and Massimo Motta's dynamic analysis of foreclosure led them to challenge the Chicago School's ideas of frequency and rationale.[76] Where there is potential competition in the downstream market and future competition in the upstream market, and these conditions remain static, a vertically integrated company does not have the incentive to engage in input foreclosure.[77] However, an analysis made using the dynamic perspective leads to a finding that input foreclosure is a logical strategy of vertically integrated firms in two cases. First, such a firm will be eager to foreclose the input if future upstream entry cannot be prevented. In such a case, the vertical incumbent will be interested in protecting its downstream monopoly and collecting rent from a more efficient upstream rival when dealing with it in the downstream market. Second, if the downstream competitor's success is a precondition for an upstream rival's entry, the incumbent vertically-integrated firm may be interested in an input foreclosure that sacrifices its immediate profits to prevent market entry upstream.[78]

Similarly, the Borkian theory of a single monopoly profit has been challenged. According to Jonathan B. Baker, this concept works in one "extreme case," when a monopolist faces neither actual nor potential competition, and buyers do not have an alternative source of supply.[79] This, as pointed out by Salop, may happen when:

(i) The upstream merging firm is an unregulated monopolist, protected by prohibitive entry barriers;
(ii) its product is used by downstream firms in fixed proportions with all other inputs; and
(iii) the downstream market is perfectly competitive.[80]

Otherwise, a dominant firm may utilize exclusionary conduct to limit the possibilities of supply from other sources, thus strengthening its market power.[81]

As an example of the anticompetitive effects of a vertical merger by a monopolist, Salop mentioned a situation in which both upstream and downstream firms are monopolists and each of them is a potential competitor of the other. Each of the companies would normally have the incentive to enter the other's market. A merger of these two firms would just petrify the existing situation characterized by the presence of two monopolists—one on an upstream and another on a downstream market. At the same time, potential new entrants would have to enter both markets simultaneously, which could result in increased risks and costs of entry.[82]

Similarly, the EDM theory has been under attack as a concept that works only in specific market conditions. For example, this could occur when a downstream firm uses inputs purchased from an upstream firm in fixed proportions with other inputs.[83] Otherwise, an unintegrated

[75]*Id.* (referring to the Frankenstein monster problem as one of the coordinated effects).

[76]*See generally* Chiara Fumagalli & Massimo Motta, *Dynamic Vertical Foreclosure*, 63 J.L. & Econ. 763 (2020).

[77]*Id.* at 799.

[78]*Id.*

[79]Jonathan B. Baker, *Taking the Error Out of "Error Cost" Analysis: What's Wrong with Antitrust's Right*, 80 Antitrust L.J. 1, 16–17 (2015). *See also* Jeffrey Church, Vertical Mergers, *in* 2 Issues in Competition Law and Policy 1455, 1469–70 (2008).

[80]Salop, *Invigorating Vertical Merger Enforcement*, *supra* note 2, at 1968–1969.

[81]Baker, *supra* note 79, at 16–17. *See* Einer Elhauge, *Tying, Bundled Discounts, and the Death of the Single Monopoly Profit Theory*, 123 Harv. L. Rev. 397, 404 (2009) (arguing that the application of single monopoly profit theory to tying practices works only in specific market circumstances, where the usage of both the tied and the tying products is fixed, the competitiveness of the tied and tying markets are fixed, and a strong positive demand correlation exists). If at least one of these conditions is not fulfilled, the profit obtained by a vertically integrated monopolist increases. *Id.*

[82]*See* Salop, *Invigorating Vertical Merger Enforcement*, *supra* note 2, at 1969.

[83]*See* Kwoka & Slade, *supra* note 46, at 52 (referring to a downstream firm being a distributor reselling products supplied by an upstream firm).

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downstream firm may substitute inputs offered for supracompetitive prices with other cheaper materials, thus reducing the penalty of being unintegrated.[84] Even if a given input is used in fixed proportions with other materials, EDM cannot be seen as an inevitable or imminent consequence of vertical integration. Steven C. Salop pointed to several such situations in which EDM may not arise. For example, when an upstream firm sells its input for a reduced price to its vertically integrated subsidiary, an "opportunity cost" arises. This in turn reduces or eliminates an incentive to reduce a downstream price. Another example is when the downstream firm would offer price reductions to a large number of existing customers relative to the number of new customers diverted from downstream competitors that did not buy the upstream firm's input. A final example is evident when the downstream firm technology is not compatible with an input produced by the upstream party to a merger.[85]

The merger specificity of EDM raises doubts as well. First, similar effects may be achieved without a merger—by way of nonlinear pricing contracts or contracts with quantity forcing.[86] Depending on the market situation, such contracts may not fully eliminate the problem of double marginalization, though their existence—or the possibility of conclusion—should be taken into consideration during the assessment of vertical merger efficiency.[87] Nonetheless, as pointed out by Salop, efficiencies resulting from EDM would not arise when foreclosure or coordination turns out to be a more profitable solution.[88] Finally, Kwoka and Slade rightly pointed out that EDM may provide only pecuniary—not real and cognizable—efficiencies, such as efficiencies resulting from the repricing of input and not from the reduction of inputs used in a production process.[89]

These post-Chicago views and claims to tighten the non-horizontal merger scrutiny met harsh criticism, mostly by the modern proponents of the Chicago school—expressed mainly in the context of mergers in digital markets. Modern proponents often emphasize the gravity of efficiencies resulting from these concentrations, including primarily EDM,[90] claiming that they should be treated in a more lenient way than horizontal mergers, or even be subject to a presumption of legality or neutrality.[91] Most of these voices are rather just a restatement of the classic arguments of the Chicago School than suggestions bringing new elements to the discussion of the vertical effects of mergers.

As evidenced by post-Chicagoans, in terms of their possible effects, vertical mergers are not entirely different from horizontal ones. Both types of mergers, depending on market circumstances, may pose intrinsic competitive harms and may lead to efficiencies.[92] Thus the claim that vertical

[84]As was proved by Fred Westfield, the penalty resulting from not being integrated decreases as product substitutability rises. *See* Fred M. Westfield, *Does Product Price Rise or Fall?*, 71 AM. ECON. REV. 334–46 (1981). Kwoka & Slade, *supra* note 45, at 52 (pointing out, rightly, that the proportion of profits and penalties of being unintegrated is ambiguous, even when an input is substitutable with other products). Typically such a substitution results in creation of a final product of slightly different characteristics, which in turn makes an assessment of such profit and penalty harder. *Id.*

[85]*See* Salop, *Invigorating Vertical Merger Enforcement*, *supra* note 2, at 1971.

[86]*Id. See also* Kwoka & Slade *supra* note 46, at 53 (giving the example of a contract in which the wholesale price is set on the level of the upstream marginal cost and overall increased profits are divided between the parties). The term "contracts with quantity forcing" generally refers to contracts containing an obligation of a buyer to purchase some threshold quantity from a supplier or contracts that reward a buyer for purchasing such a threshold quantity from him. According to the Glossary "quantity forcing on the buyer is a weaker form of non-compete, where incentives or obligations agreed between the supplier and the buyer make the latter concentrate his purchases to a large extent, but less than 80%, on the brand(s) of one supplier". See EU Commission, "Glossary of terms used in EU competition policy Antitrust and control of concentrations", 2002 (available at: https://ec.europa.eu/translation/spanish/documents/glossary_competition_archived_en.pdf).

[87]*See* Kwoka & Slade *supra* note 46, at 53.

[88]*See* Salop, *Invigorating Vertical Merger Enforcement*, *supra* note 2, at 1971.

[89]Kwoka & Slade, *supra* note 46, at 53 (stating that economic efficiency resulting from the EDM "derives entirely from output expansion, not from a decrease in unit input usage").

[90]John M. Yun, *Does Antitrust Have Digital Blind Spots?*, 72 S.C. L. REV. 305, 339 (2020); Koren Wong-Erwin, *Antitrust Analysis of Vertical Mergers: Recent Developments and Economic Teachings*, 18 ABA ANTITRUST SOURCE 3 (2019).

[91]D. Daniel Sokol, *Vertical Mergers and Entrepreneurial Exit*, 70 FLA. L. REV. 1357, 1377–78 (2018).

[92]*See* Salop, *Invigorating Vertical Merger Enforcement*, *supra* note 2, at 1973.

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integration is, in principle, pro-competitive goes much too far. Contrary to the Chicago School leaders' views, the risk of foreclosure is not illusory but real, and it occurs much more frequently than they realized. While Joe Bain's claim that vertical integration is an imminent source of implicitly exclusionary effects goes too far, there are many instances in which these effects appear. In certain market conditions, especially when at least one of the relevant markets is concentrated—but also when differentiated products are offered on a market—the risk of anticompetitive effects from vertical mergers increases significantly. These circumstances are not hypothetical, or even rare. On the contrary, industries in which differentiated products are traded are common in an economy.

Vertical integration can indeed lead to a variety of efficiencies. Some efficiencies, such as lowered transaction costs and organizational efficiencies, have been well documented by industry organizations. However, these efficiencies should be approached with caution, considering that, as both Grossman and Hart and Berle and Gardiner[93] have argued, vertical integration can lead to organizational and managerial distortions and inefficiencies. EDM must be understood as nothing more than just one of the potential efficiencies resulting from vertical mergers, neither inevitable nor automatically merger specific.

These opinions have been largely confirmed by new empirical studies by Marissa Beck and Fiona M. Scott Morton.[94] Their study provided important analysis of several dozen previous empirical studies conducted to examine the effects of vertical integration. Beck and Scott Morton's research proves that older research on the effects of vertical integration are usually not conclusive, and the results of some older studies are not directly applicable to the assessment of effects of vertical mergers on competition.[95] Although some older studies show the benefits of vertical integration—and less often, the negative effects—Beck and Scott Morton contend, "the conclusions are not robust enough to justify a procompetitive (or anticompetitive) presumption for policy purposes."[96] Of the twenty nine new studies published between 2009 and 2020 analyzed by Beck and Scott Morton, fourteen contain evidence of the harmful effects of vertical mergers and the same amount proves their beneficial consequences. Of the twenty-nine new studies published between 2009 and 2020 analyzed by Beck and Scott Morton, fourteen contain evidence of the harmful effects of vertical mergers and the same amount proves their beneficial consequences.[97] In five of these twenty-nine cases, negative and positive effects of vertical integration occurred simultaneously.[98] None of the studies, however, included a full balancing of the effects on competition, so it is hard to say what type of effect prevailed.[99] Nevertheless, analysis of these newer studies shows that vertical mergers cannot be considered as generally pro-competitive or vice versa. The overall effects of a merger depend on specific market circumstances, such as market concentration, structure, and incentives to which a company is subject.[100]

[93]Grossman & Hart, *supra* note 27, at 716. *See also* Hart & Tirole, *supra* note 31, at 206; Bolton & Scharfstein, *supra* note 27, at 112; Salop, *Invigorating Vertical Merger Enforcement*, *supra* note 2, at 1973.

[94]Marissa Beck & Fiona M. Scott Morton, *Evaluating the Evidence on Vertical Mergers*, 59 REV. IND. ORG. 273, 276 (2021).

[95]*Id.* at 276. Referring to previous studies, including that by Cooper, Froeb, O'Brien, and Vita of 2005 and Lafontaine and Slade of 2007, which are often presented as proving that vertical mergers have no negative impact on competition, Beck and Scott Morton noted that they mainly did not concern effects of concentrations but vertical restraints implemented through contractual provisions or conduct not related to merger activity, explaining their limited importance for the assessment of the effects of vertical mergers. *See generally* James C. Cooper, Luke M. Froeb, Daniel P. O'Brien, & Michael Vita, *Vertical Antitrust Policy as a Problem of Inference*, 23 INT'L J. IND. ORG. 639 (2005); Francine Lafontaine & Margaret Slade, *Exclusive Contracts and Vertical Restraints: Empirical Evidence and Public Policy, in* HANDBOOK OF ANTITRUST ECONOMICS, 391–414 (Paolo Buccirossi ed., 2008). *See also* Koren W. Wong-Ervin, *Antitrust Analysis of Vertical Mergers: Recent Developments and Economic Teachings*, 18 ANTITRUST SOURCE 1 (2019) (referring to previous empirical research as the evidence of generally procompetitive effects of vertical concentrations).

[96]Beck & Scott Morton, *supra* note 94, at 279.

[97]*Id.* at 276.

[98]*Id.*

[99]*Id.* at 289.

[100]*Id.*

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C. The U.S. Approach to Vertical Mergers

I. The Marasmus of U.S. Vertical Mergers Enforcement

Since the Chicago School paradigms dominated the American antitrust law, vertical mergers were only sporadically challenged in the USA. In the 1994–2021 period, only sixty-eight cases of such mergers were challenged by the antitrust agencies, state attorneys general, and private parties, which makes it approximately two and a half cases per year.[101] Of these sixty–eight cases, seven ended with the abandonment of the merger, three with court approval of a merger, fifty-six cases with consent decrees or final judgments imposing remedies on the parties to mergers, and one case is still pending.[102]

Enforcement by private parties almost has not existed. In just one case did private actors decide to file suit, challenging a vertical merger.[103] This comes as no surprise as the liberal approach to vertical mergers gave plaintiffs no real chance of winning a lawsuit. Little more can be said about the actions of state attorneys general who brought actions in only two cases, one jointly with the U.S. government represented by the DOJ.[104] Many of the challenged vertical mergers also posed horizontal concerns, which appear to have had a decisive influence on the results of the cases.

In the only two cases agencies challenged vertical mergers, they failed.[105] The only litigation initiated in this period by state attorneys general ended with the same result.[106] The only partially successful litigation took place in *Steves & Sons, Inc.*, initiated by a private competitor to a vertically integrated firm.[107] The district court ruled for the plaintiff by ordering divestiture of the facility purchased by the defendant and by awarding him damages.[108] On appeal, the Fourth Circuit affirmed the ruling in part related to the divestiture but vacated it in part related to the damages.[109]

Despite the increased intensity of the enforcement of vertical mergers since 2016,[110] these statistics confirm the low level of activity of both antitrust agencies and other relevant actors in the enforcement of non-horizontal mergers and acquisitions. It is worth noting that since 1994 no vertical merger has been blocked in the U.S. by an enforcement action of any kind and only in one case has divestiture of an existing merger been ordered by the court.[111]

This low level of enforcement of vertical mergers is a consequence of the application by the courts and agencies of the theories of harm based on the Chicago School of Law and Economics. The school has been skeptical about their theories possible anticompetitive effects, but rather enthusiastic about the efficiencies they may bring. This approach translates into particularly high standards of proof for plaintiffs seeking to prove an infringement, by a vertical merger, of Section 7 of the Clayton Act. This problem is demonstrated in two cases in which DOJ litigation failed. In the already famous case of *United States v. AT&T, Inc.*,[112] the DOJ argued that the merger of two heavyweight global players in the telecom and media industries, AT&T and Time Warner

[101] *See* Steven C. Salop & Daniel P. Culley, Vertical Merger Enforcement Actions: 1994–April 2020 (2020) (unpublished list) (available at https://scholarship.law.georgetown.edu/cgi/viewcontent.cgi?article=2541&context=facpub). The Salop & Culley research has been updated by the author to cover actions of enforcement finished after 2020.

[102] *Id.*

[103] *See generally* Steves & Sons, Inc. v. JELD-WEN, Inc., 345 F. Supp. 3d 614 (E.D. Va. 2018), *aff'd in part, vacated in part*, 988 F.3d 690 (4th Cir. 2021).

[104] *See generally* United States v. Republic Servs., Inc., No. 21-CV-00883, 2021 WL 3417607 (D.D.C. July 1, 2021); New York v. Deutsche Telekom AG, 439 F. Supp. 3d 179 (S.D.N.Y. 2020).

[105] United States v. AT&T Inc., 310 F. Supp. 3d 161 (D.D.C. 2018), *aff'd*, 916 F.3d 1029 (D.C. Cir. 2019); United States v. Sabre Corp., 452 F. Supp. 3d 97 (D. Del.), *vacated*, No. 20-1767, 2020 WL 4915824 (3d Cir. July 20, 2020).

[106] *Deutsche Telekom AG*, 439 F. Supp. 3d at 249.

[107] *Steves & Sons, Inc.*, 345 F. Supp. 3d at 624.

[108] *Id.* at 682.

[109] *Steves & Sons, Inc.*, 988 F.3d at 723, 725.

[110] Since the beginning of this year enforcement actions against vertical mergers have been taken in nineteen cases.

[111] *See Steves & Sons, Inc.*, 988 F.3d at 723 (ordering a divestiture of the merger).

[112] *AT&T Inc.*, 310 F. Supp. 3d at 164.

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respectively, would lead to input foreclosure in the telecom industry because AT&T would, post-merger, have preferential access to Time Warner programming for its own television service, DirecTV. The economic model presented by the DOJ to prove the likelihood of foreclosure did not convince the court because it was not based on previous real-life data.[113] Instead, the court accepted the expert testimony, which definitively showed "that prior instances of vertical integration in the video programming and distribution industry have had no statistically significant effect on content prices."[114]

Similarly, in the Sabre/Farelogix merger, the court did not accept the U.S. government's arguments that the merger would result in harm to competition due to the elimination of a maverick player offering a new innovative airfare booking system in a market dominated by three major players, including Sabre, the acquiring company. The court held that the DOJ failed to prove a reasonable probability of anticompetitive harm, including proving that barriers to entry would prevent adequate competition, and that post-merger Sabre would harm competition by eliminating Farelogix core products or raising prices.[115] Ultimately, the merger was abandoned as it had been prohibited by the UK Competition and Markets Authority ("CMA").[116] Thus, paradoxically, it was the UK competition authority, not the U.S. court, that managed to block this undoubtedly anticompetitive concentration.

The complaint filed by the FTC in July 2022, concerning the acquisition by Meta of Within, a virtual reality ("VR") content developer, could have been a harbinger of changes in this grim picture. The FTC applied to a federal court for preliminary injunctive relief to prevent the consummation of this merger.[117] The complaint, after amendment in October 2022, focused on the possible lessening of competition as a result of the integration of the successful VR fitness app offered by Within with Meta's VR business.[118] The FTC underlined that Meta already has become a key player at each level of the VR ecosystem: In hardware with its Meta Quest 2 headset, in app distribution with the Quest Store, and in apps with Beat Saber and several other popular titles.[119] The acquisition of Within has been described as an element of the wider plan of exploitation of the network-effects dynamic in VR to finally control the entire VR ecosystem.[120] As held by the FTC, Meta—instead of engaging in the competition on merits and developing its own VR fitness application—decided to eliminate one of its potential rivals.[121] The FTC claimed as well that the merger could result in lowering competitive pressure resulting from Meta's possible entry into the market for VR-dedicated fitness apps.[122] Although the court confirmed the viability of the potential competition theory of harm in the case, it held that the FTC failed to prove that the market entry was probable.[123] Thus the Court denied the FTC's motion for preliminary injunction

[113]*Id.* at 205.

[114]*Id.* at 218. *See generally* Larry Bumgardner, *AT&T and Time Warner's Vertical Merger: The Court Battle and Political Undercurrent*, 25 J.L. Bus. & Ethics 31 (2018).

[115]*Sabre Corp.*, 452 F. Supp. 3d at 97.

[116]*See* Anticipated Acquisition by Sabre Corporation of Farelogix Inc., No. ME/6806/19 (August 16, 2019) (U.K.), https://assets.publishing.service.gov.uk/media/5d8cd7d4e5274a2fb83b92d4/——_Decision_-_For_publication_pdf.pdf. However, vertical effects considerations did not determine the prohibition of the concentration by the CMA. *Id.* The CMA held that the merger raised significant competition concerns as a result of horizontal unilateral effects in the non-core Passenger Service Systems both parties supplied. *Id.* Following the abandonment of the transaction the ruling of the district court was vacated by the Third Circuit. *See* United States v. Sabre Corp., No. 20-1767, 2020 WL 4915824 (3d Cir. July 20, 2020).

[117]Complaint at 2–3, FTC v. Meta Platforms Inc., 654 F. Supp. 3d 892 (N.D. Cal. 2023) (No. 22-cv-04325).

[118]*See* Amended Complaint, FTC v. Meta Platforms Inc., 654 F. Supp. 3d 892 (N.D. Cal. 2023) (No. 22-cv-04325).

[119]*Id.* at 3, ¶ 2–4.

[120]*Id.* at 4, ¶ 6–8.

[121]*Id.* at 4, ¶ 6.

[122]*Id.* at 4–5, ¶ 5–11.

[123]*Meta Platforms, Inc.*, 654 F. Supp. 3d at 916 (discussing market entry).

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on January 31, 2023.[124] Accordingly, the FTC decided to withdraw the case. Although the court's opinion may be considered progress, overall it was a failure that called into question American antitrust agencies' reform of assessment of non-horizontal mergers. However, despite the lack of support from the judiciary, the agencies did not stop their efforts in this regard.

II. Theories of Harm and Efficiencies Applied in the Federal Courts

In the course of the development of the case law on the application of Section 7 of the Clayton Act,[125] federal courts developed several theories of harm that may be caused by vertical mergers. Of them, the biggest concern of the courts has always seemed to be the possible foreclosure of competitors from sources of supply, "input foreclosure," or the customer base, "customer foreclosure."[126]

Another theory of harm refers to the possible elimination of potential competition as a result of a merger. This theory has been structuralized into two legal doctrines of "perceived potential competition" and "actual potential competition."[127] The first of them refers to the situation in which a merger would probably eliminate a potential competitor actually exerting competitive pressure on existing market participants.[128] This perceived potential *de novo* entrant is a company that is "in the wings" of a market, ready to enter it in more favorable market conditions.[129] Accordingly, to prevent this market entry, current players tend to limit their prices and profits. Elimination of such a perceived potential entrant would normally result in the removal of this type of competitive pressure with a detriment to customers.[130] Application of the doctrine is possible only if:

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[124]*Meta Platforms, Inc.*, 654 F. Supp. 3d at 903 (denying plaintiff's motion for preliminary injunction). *See also infra* Part III.B.

[125]According to Section 7 of the Clayton Act:

> No person engaged in commerce or in any activity affecting commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital and no person subject to the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets of another person engaged also in commerce or in any activity affecting commerce, where in any line of commerce or in any activity affecting commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly. No person shall acquire, directly or indirectly, the whole or any part of the stock or other share capital and no person subject to the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets of one or more persons engaged in commerce or in any activity affecting commerce, where in any line of commerce or in any activity affecting commerce in any section of the country, the effect of such acquisition, of such stocks or assets, or of the use of such stock by the voting or granting of proxies or otherwise, may be substantially to lessen competition, or to tend to create a monopoly.

15 U.S.C. § 18.

[126]*See Brown Shoe Co.*, 370 U.S. at 323–24:

> [T]he primary vice of a vertical merger or other arrangement tying a customer to a supplier is that, by foreclosing the competitors of either party from a segment of the market otherwise open to them, the arrangement may act as a clog on competition . . . which deprive[s] . . . rivals of a fair opportunity to compete.

Id. (internal quotations omitted). *See also* Ford Motor Co. v. United States, 405 U.S. 562 (1972); United States v. E.I. du Pont de Nemours & Co., 353 U.S. 586 (1957); Heatransfer Corp. v. Volkswagenwerk, A.G., 553 F.2d 964 (5th Cir. 1977).

[127]*Meta Platforms, Inc.*, 654 F. Supp. 3d at 921. *See* United States v. Falstaff Brewing Corp., 410 U.S. 526, 559 (1973) (Marshall, J., concurring) (explaining these terms). *See also* United States v. Marine Bancorporation, Inc., 418 U.S. 602, 624 (1974) (applying *Falstaff* and further explaining "perceived potential" and "actual potential" entrants).

[128]*Id.* at 938–39 (citing *Falstaff*, 410 U.S. 559–60).

[129]*Id.* (citing Tenneco, Inc. v. FTC, 689 F.2d 346, 358 (2d Cir. 1982)). *See also Marine Bancorporation*, 418 U.S. at 624–25 (recognizing the "wings effect").

[130]*See Marine Bancorporation*, 418 U.S. at 624–25:

> [T]he principal focus of the doctrine is on the likely effects of the premerger position of the acquiring firm on the fringe of the target market . . . In other words, the Court has interpreted § 7 [of the Clayton Act] as encompassing what is commonly known as the wings effect—the probability that the acquiring firm prompted premerger

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> [T]he target market is substantially concentrated, if the acquiring firm has the characteristics, capabilities, and economic incentive to render it a perceived potential *de novo* entrant, and if the acquiring firm's premerger presence on the fringe of the target market tempered oligopolistic behavior on the part of existing participants in that market.[131]

In addition to the degree of market concentration, the courts were analyzing numerous other elements including barriers to entry, the capability of the perceived potential entrant, its incentive to entry, and the possibility of other market entries.[132]

The doctrine of the actual potential entrant is centered around the elimination of the likelihood, absent a merger, of a potential entry into a strongly concentrated market resulting from possible internal growth of a company, a "*de novo* entry," or by the acquisition of another small existing player, a "toe-hold acquisition."[133] Here, the attention of a court is focused not on the competitive pressure exerted on existing operators perceiving a market entry, but on the effects that the lack of such an entry may have on competition in this market.

The establishment of foreclosure based on the actual potential entry doctrine requires proof of a highly concentrated market, availability of other feasible means for entering the market by a possible entrant, *de novo* or by toe-hold acquisition, and that those means offer a substantial likelihood of ultimately producing deconcentration of that market or other significant procompetitive effects.[134] Because, as the Supreme Court held in *Brown Shoe Co.*, Section 7 deals in "probabilities," not "ephemeral possibilities,"[135] the actual potential entry doctrine has always been consciously applied by the courts.[136] In a recent Meta/Within merger case, the Northern District of California confirmed that the actual potential entry is a viable merger assessment doctrine.[137] At the same time, the court held that for the plaintiff it is enough to prove that the market entry of the acquiring firm would have been "reasonably probable."[138]

Another theory of harm admittedly applied more frequently to conglomerate mergers, refers to a significant rise in barriers to entry or the effective competition being the effect of a merger.[139] This so-called entrenchment theory is centered around the notion of a merger party's acquiring a substantial competitive advantage resulting in raising barriers to entry or barriers to effective competition. Such advantages may cover lower advertising costs,[140] distribution efficiencies,[141]

> procompetitive effects within the target market by being perceived by the existing firms in that market as likely to enter *de novo* . . . . The elimination of such present procompetitive effects may render a merger unlawful under § 7.

Id. (internal quotations omitted) (citing *Falstaff*, 410 U.S. at 531–37).

[131]*Marine Bancorporation*, 418 U.S. at 624–25. *See also Falstaff*, 410 U.S. at 531–37. Usually, the courts have required a relatively high degree of market concentration to enjoin a merger. *See id.* at 538 (finding the appropriate degree of market concentration when the sum of the market shares of the four largest operators at the level of 61.3%). A similar share of the largest four competitors was found to be sufficient in other cases. *See United States v. Phillips Petroleum Co.*, 367 F. Supp. 1226, 1253 (C.D. Cal. 1973) (affirming judgment); *Tidewater Oil Co. v. United States*, 418 U.S. 906 (1974); *United States v. Wilson Sporting Goods Co.*, 288 F. Supp. 543 (N.D. Ill. 1968).

[132]*See* William Holmes & Melissa Mangiaracina, Antitrust Law Handbook § 6:7 (2023–2024 ed.).

[133]*Marine Bancorporation*, 418 U.S. at 625–26.

[134]*Id.* at 633.

[135]*Brown Shoe Co.*, 370 U.S. at 323.

[136]*See, e.g.*, *Meta Platforms, Inc.*, 654 F. Supp. 3d at 925 (explaining how the Supreme Court has "declined to resolve the doctrine's validity" and collecting cases of the doctrine's cautious application).

[137]*Id.* at 926–27.

[138]*Id.* at 931.

[139]*See Ford Motor Co.*, 405 U.S. at 562; FTC v. Procter & Gamble Co., 386 U.S. 568 (1967); Gen. Foods Corp. v. FTC, 386 F.2d 936 (3d Cir. 1967); United States v. Standard Oil Co., 253 F. Supp. 196 (D.N.J. 1966).

[140]*See Procter & Gamble Co.*, 386 U.S. at 568 (prohibiting the conglomerate merger between Clorox and Procter & Gamble and concluding that advantages resulting from combining these firms' promotional and advertising assets might have raised high barriers to entry on the bleach market already dominated by Clorox). *See also Gen. Foods Corp.*, 386 F.2d at 936.

[141]*Wilson Sporting Goods Co.*, 288 F. Supp. at 568.

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a favorable position to finance a firm's operations,[142] the potential to offer a complete line of products,[143] extending consumer financing to prospective purchasers,[144] and reciprocal dealing.[145]

Theories of harm developed by the court in classic cases adjudicated before the Chicago School paradigm shift, including *Brown Shoe Co.*,[146] *Ford Motor Co.*,[147] or *Marine Bancorporation, Inc.*[148] are not currently applied in practice. Due to the high burden of proof imposed on plaintiffs, attempts to challenge vertical mergers are usually doomed to failure. This makes the U.S. vertical merger enforcement toothless. Agencies, state attorneys general, and private plaintiffs rarely resort to litigation, rightly being afraid of failure. Acting rationally, the Agencies tend to impose remedies in consent decrees.[149] In extreme cases, the agencies may be more inclined to issue a consent order, even if it does not fully remove the threat to competition than to bring legal action for a permanent injunction from a merger.[150]

III. Theories of Harm and Efficiencies Contained in the 2020 U.S. Vertical Merger Guidelines

In 2020, the DOJ and the FTC decided to adopt the U.S. 2020 VM Guidelines,[151] which were to replace the still applicable provisions of the 1984 Merger Guidelines[152] concerning the assessment of non-horizontal mergers. This was a long-awaited step. Unlike the horizontal part of the 1984 Merger Guidelines, which were amended in 1992 and 1997 and then replaced in 2010,[153] the non-horizontal part remained in force and unchanged for almost forty years and was generally considered outdated. However, the U.S. 2020 VM Guidelines did not meet the expectations of those who proposed a complete departure from Chicago paradigms and a significant tightening of the vertical merger policy.[154] Anyway, they have not played a significant practical role.

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[142]*See* United States v. Ingersoll-Rand Co., 320 F.2d 509 (3d Cir. 1963). *But see* United States v. FMC Corp., 84 S. Ct. 4 (1963).

[143]*See Gen. Foods Corp.*, 386 F.2d at 936. *See also Ingersoll-Rand Co.*, 320 F.2d at 509. *But see FMC Corp.*, 84 S. Ct. at 4.

[144]*See Ingersoll-Rand Co.*, 320 F.2d at 509. *But see FMC Corp.*, 84 S. Ct. at 4.

[145]"Reciprocal dealing" means the situation in which one of the parties has sales or purchasing leverage over other market players purchasing products that the other party to the merger offers. *See* FTC v. Consolidated Foods Corp., 380 U.S. 592 (1965); *Gen. Foods Corp*, 386 F.2d 936.

[146]*Brown Shoe Co.*, 370 U.S. at 294.

[147]*Ford Motor Co.*, 405 U.S. at 562.

[148]*Marine Bancorporation*, 418 U.S. at 602.

[149]According to Ginsburg and Wright, the DOJ resolved nearly its entire antitrust civil enforcement docket by consent decree from 2004 to 2012 and the FTC has settled 93 percent of its competition cases with consent decrees between 1995 and 2012. See: Douglas H. Ginsburg & Joshua D. Wright, Antitrust Settlements: The Culture of Consent in William E. Kovacic: An Antitrust Tribute – Liber Amicorum (Vol. I) (Charbit et al. eds., February 2013) George Mason University Law and Economics Research Paper Series, 13-18.

[150]See for example the FTC consent orders: of December 29, 2000, In the Matter of The Boeing Company, a corporation. Docket No. C-3992; and of August 17, 2017, In the Matter of Broadcom Limited, a limited company, and Brocade Communications Systems, Inc. a corporation. Docket No. C-4622.

[151]*See generally* DEP'T OF JUST. & FED. TRADE COMM'N, VERTICAL MERGER GUIDELINES (2020) [hereinafter U.S. 2020 VM Guidelines].

[152]1984 MERGER GUIDELINES OF 1984, *supra* note 7, at 23–28.

[153]*See generally* U.S. 2010 HORIZONTAL MERGER GUIDELINES, *supra* note 70.

[154]*See* Steven C. Salop, *A Suggested Revision of the 2020 Vertical Merger Guidelines*, 67 ANTITRUST BULL. 371, 371–89 (2022); James Keyte, *The Draft Vertical Merger Guidelines: A Modern Approach, But Gaps and Questions Remain*, 34 ANTITRUST BULL. 5, 6–7 (2020). *See also* Statement from Lina M. Khan on the Withdrawal of the Vertical Merger Guidelines 2 (Sept. 15, 2021), https://www.ftc.gov/system/files/documents/public_statements/1596396/statement_of_chair_lina_m_khan_commissioner_rohit_chopra_and_commissioner_rebecca_kelly_slaughter_on.pdf. However, there were also opinions criticizing the U.S. 2020 VM Guidelines for ambiguity, for relying on misleading and unclear economic concepts and for too restrictive of an approach. *See* Brianna L. Alderman & Roger C. Blair, *The 2020 Vertical Merger Guidelines: Some Suggestions for Revision*, 67 ANTITRUST BULL. 390, 390–405 (2022).

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Among the anticompetitive effects of vertical mergers, the U.S. 2020 VM Guidelines mentioned the unilateral effects including foreclosure, raising rivals' costs and access to competitively significant information, and the vulnerability of a relevant market to coordinated conduct.[155] First, to establish a foreclosure, the agencies would check whether the merged firm would likely be able to cause those rivals to lose significant sales in the relevant market or to otherwise compete less aggressively for customers' business.[156] Second, the agencies would check whether a reduction in actual or potential competition with users of the related product in the relevant market would be profitable for the merged firm.[157]

The Guidelines referred quite extensively to possible procompetitive effects of vertical mergers holding first that they "combine[d] complementary economic functions and eliminate[d] contracting frictions and therefore ha[d] the capacity to create a range of potentially cognizable efficiencies that benefit[ted] competition and consumers."[158] The Guidelines mentioned improvements in production, inventory management, distribution, or the creation of new innovative products. To be considered cognizable, efficiencies must have been merger-specific, verifiable, and not arising from anticompetitive reductions in output or service.[159] A merger leading to cognizable efficiencies of gravity and character such as it was "unlikely to be anticompetitive in any relevant market" was normally not challenged.[160]

According to the Guidelines, EDM was "not a production, research, and development, or procurement efficiency; it ar[ose] directly from the alignment of economic incentives between the merging firms."[161] Due to EDM, vertical mergers "often result[ed] in the merged firm's incurring lower costs for the upstream input than the downstream firm would have paid absent the merger."[162] The agencies would verify the EDM typically by examining the likely savings resulting from self-supplying inputs following a vertical merger. EDM might still have been considered merger-specific even if a similar effect could theoretically be achieved absent the merger, provided that such practices were not evidenced in documents.

The U.S. 2020 VM Guidelines referred to market structure as one of the possible assessment criteria for the effects of mergers. However, the agencies did not have to but only might have "consider[ed] measures of market shares and market concentration in a relevant market in their evaluation of competitive effects."[163] The guidelines did not provide a safe harbor rule based on the market share or Herfindahl-Hirschman Index ("HHI") thresholds.

Summing up, the theories of harm and the assessment schemes were described in the U.S. 2020 VM Guidelines in a rather general manner, which on the one hand allowed for high flexibility in their application, and on the other hand, made it difficult to assess the legal solutions contained therein. There is no doubt, however, that the U.S. 2020 VM Guidelines represented a significant improvement as compared to the 1984 Merger Guidelines. Their content showed that the risk of foreclosure and other negative effects were not considered to be illusory, but to be a real consequence of vertical mergers.

The U.S. 2020 VM Guidelines were based on the right assumption that foreclosure was the primary competition concern arising from vertical mergers. This is confirmed by the agencies' practice. In the overall number of enforcement actions taken in the 1994–2021 period, foreclosure was the theory of harm most frequently applied by the agencies in fifty–three of sixty-eight cases. The theories of harm based on the elimination of potential competition were applied in nine cases;

[155]U.S. 2020 VM Guidelines, *supra* note 151, at 4.
[156]*Id.* at 4.
[157]*Id.* at 5.
[158]*Id.* at 11.
[159]*Id.*
[160]*Id.*
[161]*Id.*
[162]*Id.*
[163]*Id.* at 3.

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the theories based on misuse of sensitive information, in twenty-two cases; and those based on coordination resulting from information exchange, in thirteen cases.[164]

But, the theories of harm contained in the U.S. 2020 VM Guidelines seemed to lack certain important elements. First, the Guidelines appeared to pay too little attention to the structure of the market, including market concentration and the market share of the parties to the merger. These factors were decisive for the risk of negative effects of vertical concentrations on the competition. While the absence of the safe-harbor threshold allowed the agencies to flexibly assess the negative consequences of vertical mergers, it was worth developing the rebuttable presumption of the anticompetitive effects of such mergers on highly concentrated markets. Second, the U.S. 2020 VM Guidelines, as opposed to the 1984 Merger Guidelines, did not take into account the importance of the parties' activities in markets where differentiated products were offered for the assessment of foreclosure risk.

However, it was not the description of theories of harm, but the part devoted to the potential positive effects of vertical mergers that raised the biggest reservations. The U.S. 2020 VM Guidelines rightly held that, depending on the circumstances, vertical mergers could or could not lead to economic efficiencies. However, this did not apply to the EDM. It was considered to be a natural and automatic consequence of vertical mergers influencing the downstream market prices, rather than just efficiency. The 2020 guidelines recognized that every vertical merger resulted in the EDM, although benefits resulting from it did not in every case outweigh any negative effects on competition resulting from such a merger. Still, even where a similar effect could be achieved by means other than a merger, the EDM was considered an efficiency resulting from a merger. Such a concept of the EDM clearly contradicted the post-Chicago scholars' views presented above and became a main subject of the criticism of then-newly appointed heads of U.S. antitrust authorities.

On September 15, 2021, the FTC voted three-to-two to withdraw its approval of the U.S. 2020 VM Guidelines.[165] In its statement, the FTC concluded that the Guidelines were based on "unsound economic theories that [we]re unsupported by the law or market realities"[166] and that the decision to withdraw the Guidelines was made "in order to prevent industry or judicial reliance on a flawed approach."[167] It was not the theories of harm provided in the Guidelines that were criticized by the Commission, but its approach to efficiencies, which, according to the FTC, were not recognized by the statute as a defense to an unlawful merger and thus "improperly contravened the Clayton Act's language."[168] As the majority of Commissioners concluded, the Guidelines' "flawed discussion of the purported procompetitive benefits (i.e., efficiencies)) of vertical mergers, especially its treatment of the elimination of double marginalization ("EDM"), could become difficult to correct if relied on by courts."[169] At the same time, the DOJ decided to continue the application of the U.S. 2020 VM Guidelines.

In January 2022, both U.S. antitrust agencies launched a joint initiative of comprehensive reviewing of merger guidelines, starting from the joint public inquiry aimed at modernizing both horizontal and vertical merger guidelines.[170] The inquiry focused on the most fundamental

[164]*See* Steven C. Salop & Daniel P. Culley, *Revising the US Vertical Merger Guidelines: Revising the U.S. Vertical Merger Guidelines: Policy Issues and an Interim Guide for Practitioners* 4 J. ANTITRUST ENF'T 1 (2015); Daniel Gross, *Is Vertical Integration Making a Comeback?*, STRATEGY & BUS. BLOG (Dec. 2, 2021), https://www.strategy-business.com/blog/Is-vertical-integration-making-a-comeback.

[165]*See* Press Release, Fed. Trade Comm'n, Federal Trade Commission Withdraws Vertical Merger Guidelines and Commentary (Sept. 15, 2021), https://www.ftc.gov/news-events/news/press-releases/2021/09/federal-trade-commission-withdraws-vertical-merger-guidelines-commentary.

[166]*Id.*

[167]*Id.*

[168]*Id.*

[169]Statement from Lina M. Khan, *supra* note 154, at 2.

[170]*See* Press Release, Fed. Trade Comm'n, Federal Trade Commission and Justice Department Seek to Strengthen Enforcement Against Illegal Mergers (Jan. 18, 2022), https://www.ftc.gov/news-events/news/press-releases/2022/01/federal-trade-commission-justice-department-seek-strengthen-enforcement-against-illegal-mergers/.

https://doi.org/10.1017/glj.2024.44 Published online by Cambridge University Press

challenges of modern merger enforcement including threats to potential and nascent competition and those specifically related to digital markets.[171]

I. *U.S. 2023 Merger Guidelines*

In July 2023, both U.S. antitrust agencies published a draft of new merger guidelines for comment purposes.[172] The draft contained thirteen guidelines that corresponded to the general assumptions on which the proposed approach to mergers was supposed to be based. "Guideline 6: Vertical Mergers Should Not Create Market Structures That Foreclose Competition" applied to vertical mergers. Already from its wording, it was clear that the U.S. antitrust agencies proposed a greater focus on structural factors. Further, the agencies emphasized that the assessment of the impact of vertical mergers on competition might include a structural analysis of a supply chain aimed at examining the impact of concentration on the restructuration of a vertical supply or distribution chain.[173] According to the draft guidelines, the primary concern of vertical mergers was possible foreclosure, which might operate as "a clog on competition, which deprives rivals of a fair opportunity to compete."[174]

The agencies, therefore, proposed a rebuttable presumption that a vertical merger might substantially lessen competition if a party holds 50% of the "foreclosure share."[175] In such a situation, "market structure alone indicates the merger may substantially lessen competition."[176] The draft provided the list of defenses that could rebut the presumption of foreclosure, including the failing firm defense, facilitation of market entry, and procompetitive efficiencies. The defenses were supposed to be limited to the relevant market, merger-specific, and verifiable.[177] When the foreclosure share was less than 50%, the agencies would consider both the foreclosure share as such and relevant plus factors.[178]

This far-reaching concept, however, did not survive in the same form. In the final version of the U.S. 2023 Merger Guidelines, published in December 2023, the agencies did not retain Guideline 6 containing the structural presumption of illegality of a merger based on the foreclosure share threshold. Instead, Guideline 5 concerning limiting access to products or services that a merged firm's rivals use to compete, has been changed, and supplemented with rules on vertical mergers.

As amended, Guideline 5 concerns limiting rivals' access to products and services in relation to all types of mergers, whether or not they involve a traditional vertical relationship. The Guideline focuses on foreclosure as the primary concern though mentions two other theories of harm—getting access to rivals' competitively sensitive information and deterring rivals from entering the market in response to a possible foreclosure by the merged firm.[179]

Within the scope of the analysis of the risk of limiting access to products and services, the agencies take into consideration the ability and incentive of the merged firm to foreclose rivals. In this assessment, they focus on the availability of substitutes for the related product, its competitive significance, the effect of a merger on competition in the relevant market, and the intensity of competition between the merged firm and the dependent firms.

When examining these factors, the agencies use the standard analytical, economic, and evidentiary toolbox supplemented however with additional considerations and evidence related to

[171]Press Release, Dep't of Just. & Fed. Trade Comm'n, Request for Information on Merger Enforcement (Jan. 18, 2022), https://downloads.regulations.gov/FTC-2022-0003-0001/content.pdf.

[172]Dep't of Just. & Fed. Trade Comm'n, Draft Merger Guidelines (2023).

[173]*Id.* at 3.

[174]*Id.* at 17.

[175]*Id.*

[176]*Id.* at 3, 17.

[177]*Id.* at 31–34.

[178]*Id.* at 17.

[179]*Id.* at 2.

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barriers to entry and exclusion of rivals, including the necessity of multi-level entry; foreclosure as a result of prior transactions or actions of merged firms; and market structure. The additional considerations and evidence provide insight into the availability of substitutes and the competition in the market for the related product or the relevant market. Moreover, the incentive to foreclose can be identified in the internal documents of merged firms.

Much attention has been paid to the analysis of elements external to the merged firm such as industry factors and market structure. The agencies analyze both related and relevant market structures. In the framework of the former, the agencies take into account the foreclosure share, the same on which the presumption contained in Guideline 6 of the Draft Guidelines was based.[180] The "foreclosure share" is the share of the related market to which the merged firm could limit access.[181] That is controlled by the merged firm, such that it could foreclose the rival's access to the related product on competitive terms. The "related market" is understood as a market defined around the related product, that is, any product, service, or route to market that rivals use to compete in that market.[182] The concept of the related product covers *inter alia* products rivals currently or may in the future use as inputs, products that provide distribution services for rivals or otherwise influence customers' purchase decisions, products that provide or increase the merged firm's access to competitively sensitive information about its rivals, or complements that increase the value of rivals' products.[183]

Although the Guidelines do not establish a presumption based explicitly on the percentage of the foreclosure share, they recognize that a high share in a market for a competitively significant related product showing that "the merged firm is approaching or has monopoly power" over this product is "a sufficient basis to demonstrate that the dependent firms do not have adequate substitutes and the merged companies have the ability to weaken or exclude them by limiting their access to the related product."[184] At the same time, the agencies confirmed, citing *Brown Shoe Co.*,[185] that by sufficiently high, they mean a share greater than 50% of the related product market.[186] The guidelines also indicate that "a merger involving a related product with share of less than 50% may still substantially lessen competition, particularly when that related product is important to its trading partners."[187]

When assessing the probability of foreclosure, the agencies also consider the structure of the relevant market, including its share, and concentration measures. The less intensive the competition is in the market, the greater the anticompetitive effect is. Moreover, "the merged firm has a greater incentive to limit access to the dependent firms when it competes more closely with them."[188] The agencies also take into account the actual vertical integration of firms in the relevant and related markets as well as the general trend toward further vertical integration.[189]

This trend is also taken into account in the application of Guideline 7 which is focused on the question of whether an industry's trend toward consolidation increases the risk a merger is anticompetitive.[190] Here, the agencies consider the recent history and likely trajectory of an industry, including not only a trend toward horizontal, but also vertical integration. If a merger is part of such a trend, its significance for the future competitive dynamics of the industry is

[180]*Id.*
[181]*Id.*
[182]*Id.* at 17.
[183]*See generally* U.S. 2023 Merger Guidelines, *supra* note 11.
[184]*Id.* at 16.
[185]*Brown Shoe*, 370 U.S. at 294.
[186]*See* U.S. 2023 Merger Guidelines, *supra* note 11, at 16.
[187]*Id.*
[188]*Id.*
[189]*See id.*
[190]*See id.* at 22.

https://doi.org/10.1017/glj.2024.44 Published online by Cambridge University Press

examined. A merger of this type may reinforce the concerns addressed in Guideline 5, in particular those of making entry at a single level more difficult.[191]

According to the U.S. 2023 Merger Guidelines, companies may present rebuttal arguments, including that the merger would lead to vertical integration of complementary products and as a result, "eliminate double marginalization."[192] However, EDM can only take place "in specific circumstances."[193] The agencies' task is to verify whether EDM meets the conditions set out in the Guidelines for all efficiencies, such as merger specificity, verifiability, preventing a reduction in competition, and being not anticompetitive. In the framework of this evaluation, the agencies examine: (i) Whether the merged firm will be more vertically integrated as a result of the merger, for example because it increases the extent to which it uses internal production of an input when producing output for the relevant market; (ii) whether contracts short of a merger have eliminated or could eliminate double marginalization such that it would not be merger-specific; and (iii) whether the merged firm has the incentive to reduce price in the relevant market given that such a reduction would reduce sales by the merged firm's rivals in the relevant market, which would in turn lead to reduced revenue and margin on sales of the related product to the dependent rivals.[194]

The U.S. 2023 Merger Guidelines make it clear that the agencies will assess efficiencies carefully. The assessment will be based on the assumption that "firms act to maximize their overall profits and valuation rather than the profits of any particular business unit."[195] All claims by merging firms must be supported by an objective analysis.[196]

The new standard of assessment of vertical mergers established in the U.S. 2023 Merger Guidelines reflects the post-Chicago School concepts presented earlier in this text. Here, foreclosure is considered the major concern of the agencies, and its perspective is understood as the potentially real, not hypothetical, consequence of vertical mergers. In the complex assessment of the likelihood of foreclosure, an important place has been reserved for market structure analysis, which echoes the Neo-Brandeisians' ideas focused on existing and trending market structures.

Although the final U.S. 2023 Merger Guidelines, unlike the Draft Guidelines, do not introduce a presumption of significant lessening of competition by a merger, explicitly based on a specific market share ceiling, structural factors are still crucial in merger assessment. It must be noticed, that the impact not only on the structure of the market in which the concentration parties operate but also on the structure of all "related markets" is examined. This is a comprehensive view, in which concerns about the development of oligopolistic and monopolistic market structures, including those based on vertical integration, play an important role. The introduction of a presumption of the anticompetitive nature of vertical merger based on a high share in a related product market is a slightly more modest solution than the one contained in the Draft Guidelines. Still, high market share alone may determine the *prima facie* anticompetitiveness of a merger. Moreover, this type of presumption allows for more flexibility in merger assessment. This solution, being the opposite of the safe harbor established in the EU NHM Guidelines, seems to be the most significant change concerning vertical mergers implemented by the U.S. 2023 Merger Guidelines. This reflects the agencies' view that the anticompetitive potential of vertical mergers is comparable to the potential of horizontal ones.

Another novelty concerns the perception of efficiency, which could outweigh the anticompetitive effects of a vertical merger. All the potential efficiencies, including EDM,

[191]*See id.* at 16.
[192]*Id.*
[193]*Id.*
[194]*Id.*
[195]*Id.*
[196]*See id.* at 16–17.

https://doi.org/10.1017/glj.2024.44 Published online by Cambridge University Press

are to be not only viable but also merger-specific, and the benefits resulting from them cannot be limited to the parties but must be adequately transferred to customers. Therefore EDM is no longer treated as an automatic consequence of vertical mergers.

D. The EU Non-horizontal Merger Guidelines—A Call for Changes?

The Commission's 2008 Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings (hereinafter referred to as the EU NHM Guidelines) are a much more extensive piece of legislation than their American counterpart.[197] They refer separately to vertical and conglomerate mergers and describe their possible effects and methods of assessment much more comprehensively and thoroughly than the latter.

The EU NHM Guidelines expressly state that "non-horizontal mergers are generally less likely to significantly impede effective competition than horizontal mergers."[198] This is because non-horizontal mergers do not entail the loss of direct competition between the merged firms. The EU NHM Guidelines seem to overestimate the procompetitive nature of vertical concentrations and underestimate their potential negative effects. The statement that non-horizontal mergers are generally less likely to significantly impede effective competition than horizontal mergers, goes too far and is not confirmed by empirical research and economic theories. In light of the current state of economic research presented above, this position has no justification and should be removed from the Guidelines. There is a need to reformulate the EU NHM Guidelines' overall rhetoric on the possible effects of non-horizontal mergers to change the impression that one may have reading them, that vertical mergers are generally less harmful than horizontal mergers and usually lead to significant economic efficiencies.

Admittedly, in contrast to the U.S. 2023 Merger Guidelines, the EU NHM Guidelines contain a safe harbor rule for mergers between parties not having significant market power. As the Commission underlined, non-horizontal mergers pose a threat to competition only when the merged undertaking has a significant degree of market power in at least one of the markets. Accordingly, concentrations that lead to a market share of less than 30% and HHI below 2000 will not normally be extensively investigated by the Commission.[199] This does not however refer to mergers where one or more special circumstances are present, including for instance where:

a) a merger involves a company that is likely to expand significantly in the near future, for example, because of a recent innovation;
b) there are significant cross-shareholdings or cross-directorships among the market participants;
c) one of the merging firms is a firm with a high likelihood of disrupting coordinated conduct;
d) indications of past or ongoing coordination, or facilitating practices, are present.[200]

Because the structure of markets in which parties to a concentration are active, the level of these markets' concentration and market shares of the parties seem to be crucial elements of the assessment of possible negative effects of vertical mergers, the EU NHM Guidelines rightly attach big importance to them. This quasi, almost, safe harbor established in the EU NHM Guidelines should not raise such concerns as were related to the proposal to include a similar solution in the U.S. 2020 VM Guidelines. The exceptions from the presumption of compatibility of a

[197]*See generally* Commission Guidelines on the Assessment of Non-Horizontal Mergers Under the Council Regulation on the Control of Concentrations Between Undertakings, 2008 O.J. (C 265) (EU) [hereinafter EU NHM Guidelines].
[198]*Id.* ¶ 11.
[199]*Id.* ¶ 25.
[200]*Id.* ¶ 26.

https://doi.org/10.1017/glj.2024.44 Published online by Cambridge University Press

concentration with the internal market provided in the EU NHM Guidelines, based on market share and HHI thresholds, are formulated in such a way as to give the flexibility needed to exercise control over all kinds of potentially anticompetitive non-horizontal mergers notified to the Commission. Moreover, it must be taken into consideration that the list of these exceptions is not exhaustive.

But first, this approach still reflects the belief that vertical concentrations are less harmful than horizontal concentrations. Safe harbor in the case of horizontal concentrations is based on lower thresholds and applies where the market share of the obligations concerned does not exceed 25% either in the common market or in a substantial part of it, or if a post-merger HHI is below 1000.[201] Accordingly, taking into account the foregoing considerations regarding the relevance of the market structure as one of the criteria for the assessment of the competitive effects of vertical mergers, the implementation of thresholds of market shares and market concentrations as a basis for a rebuttable presumption of anticompetitive effects of mergers could be taken into consideration. The establishment of such thresholds could give a clear signal of more tightened vertical concentrations' scrutiny.[202]

Second, unlike under the U.S. 2023 Merger Guidelines, the market share thresholds refer to the relevant market, not the foreclosure share. The advantage of this solution is that the safe harbor is based on one of the most developed concepts of competition law, the meaning of which is established both by case law and scholarship. This increases the level of legal certainty, making it easier for parties to predict the Commission's decision. However, the market share criterion does not sufficiently reflect the foreclosure potential of an agreement. Therefore, a dissonance arises between the theories of harm contained in the EU NHM Guidelines and the construction of the safe harbor. The former has been outlined relatively broadly and allows for a relatively complex assessment of the possibilities of foreclosure, including factors to which, under the U.S. 2023 Merger Guidelines, the concept of "related products" refers, such as access to competitively sensitive information described below. The latter is based on a much narrower concept of the parties' relevant market shares. In this context, the proposal formulated by American antitrust agencies, assuming a rebuttable presumption based on the high "foreclosure share," deserves approval and is worth transplanting into the EU law. An alternative, although worse solution, is to decrease the current post-merger thresholds for relevant market share and HHI to the level that applies to horizontal concentrations.

Similar to the U.S. 2023 Merger Guidelines, EU NHM Guidelines perceive foreclosure as the main potential threat to competition resulting from vertical mergers. Like under the U.S. 2023 Merger Guidelines the assessment scheme focuses first on the analysis of the ability and incentive to foreclose. However, the effects that foreclosure may have on competition are analyzed in the EU NHM Guidelines in a much more extensive way and separately for input and consumer foreclosure.[203] Under the U.S. 2023 Merger Guidelines, these effects are analyzed jointly, which is made possible by the concept of the "related product" described above.

The 2023 U.S. Merger Guidelines do not provide for specific theories of harm for vertical mergers but, in a rather general manner, refer to foreclosure as the most serious possible effect of them. In describing the factors considered while assessing the propensity of a merger to foreclose, the agencies focus mainly on structural factors including an existing concentration in the markets, both relevant and related; the current situation; and overall trends in vertical integration. They also look at the possibility of raising barriers to trade and purpose to foreclose rivals.

[201]Commission Guidelines on the Assessment of Non-Horizontal Mergers Under the Council Regulation on the Control of Concentrations Between Undertakings, 2004 O.J. (C 31).

[202]The EU NHM Guidelines require also the development of a comprehensive scheme of assessment of non-horizontal mergers of undertakings active on non-price or attention markets. This however is beyond the scope of this Article.

[203]*See* EU NHM Guidelines, *supra* note 197, ¶ 29–77.

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As was in the case of the U.S. 2020 VM Guidelines, their EU counterpart focuses on possible alternatives for customers buying inputs, "input foreclosure," or sufficient economic alternatives in the downstream market for the upstream rivals, "actual or potential," to sell their output, "customer foreclosure."[204] The U.S. 2023 Merger Guidelines are much more restrained and limit themselves to the assessment of the availability of substitutes for the related product. According to the EU NHM Guidelines on the framework of the assessment of the ability to foreclose, the Commission analyzes the market power and structure of the relevant markets concerned, as well as possible rivals' reactions to a price hike and their potential counter-strategies.[205]

In the framework of the incentive to foreclose analysis, the Commission takes into account "the degree to which foreclosure would be profitable" which means the assessment of the results of the trade-off between the profit lost due to the reduction of input to downstream rivals, "input foreclosure," or due to not procuring products from upstream rivals, "customer foreclosure," and the possible gains from continuing these supplies or procurements.[206] The U.S. 2023 Merger Guidelines however do not refer to the profitability of foreclosure as such but rather place it in the context of the factors that are normally assessed by the agencies and, that may influence the foreclosure profitability, such as the availability of substitutes and competition between the merged firm and the dependent firms.

Finally, the Commission assesses the overall likely impact on effective competition, that is, whether a merger may lead to increased prices or reduced output on the downstream market by raising pressure on sales prices, "input foreclosure," or by reducing the upstream rivals' ability to compete, "customer foreclosure."[207] The Commission focuses on the proportion of foreclosed rivals, their role in a relevant market, and the share of the input or output affected. The Commission concentrates as well on the likelihood of raising entry barriers. Finally, the possible countervailing factors are being assessed, including the likelihood of market entry and possible efficiencies resulting from a merger.

Similar to the U.S. 2023 Merger Guidelines, their EU counterpart mentions gaining access to commercially sensitive information regarding the upstream or downstream activities of rivals as another possible unilateral, "non-coordinated," anticompetitive effect of vertical mergers.[208]

The EU NHM Guidelines refer to the possible coordinated effects of vertical concentrations in a similar, but much more extensive manner, to the U.S. 2023 Merger Guidelines. Compared to the latter, the EU NHM Guidelines put more emphasis on market characteristics, incentives, and the ability to cooperate. The EU Guidelines thus underline that reaching terms of coordination post-merger may *eo ipso* result from a reduction in the number of effective competitors, an increase in the degree of symmetry or transparency between market players, or the elimination of a maverick firm. Furthermore, the EU NHM Guidelines mention three conditions for sustainable coordination, that is: (i) The coordinating firms must be able to monitor to a sufficient degree whether the terms of coordination are being adhered to; (ii) discipline requires that there is some form of deterrent mechanism that can be activated if a deviation is detected; and (iii) the reactions of outsiders should not be able to jeopardize the results expected from the coordination.[209]

The theories of harm contained in the EU NHM Guidelines are not sufficiently developed and do not reflect all the complexity of factors that may affect the anticompetitive character of a merger. This refers primarily to the impact that activity in a market in which differentiated products are offered may have on a competitive assessment of vertical mergers.

[204] *Id.* ¶ 30.
[205] *See id.* ¶ 39, 67.
[206] *See id.* ¶ 40.
[207] *See id.* ¶ 47–57, 72–77.
[208] *See id.* ¶ 78.
[209] *Id.* ¶ 81.

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Although EU NHM Guidelines consider market structure to be one of the important factors taken into account while assessing the foreclosure potential of a merger, they neglect another of the most important elements—an overall trend of vertical integration and concentration of relevant and related markets.

Due to these reservations, it is necessary to introduce appropriate adjustments to the EU NHM Guidelines. First and foremost, they should cover modification of the assessment of the possibility of foreclosure by supplementing it with the criterion of the differentiated nature of products offered on relevant markets. The evidence of this should be treated as one of the factors that significantly increases the risk of anticompetitive foreclosure. Second, the merger compatibility assessment should be focused on the identification of an overall trend to foreclose existing in a relevant or a related market and the general purpose of the parties to foreclose the rivals.

The most significant differences between the EU NHM Guidelines and the U.S. 2023 Merger Guidelines arguably concern the assessment of efficiencies resulting from non-horizontal mergers. The EU NHM Guidelines are based on similar assumptions as compared to their US counterpart, according to which anticompetitive effects of a merger are balanced against its efficiencies. The Commission analyzes whether the efficiencies (1) benefit consumers, (2) are merger-specific, and (3) are verifiable.[210] Similarly to the U.S. 2023 Merger Guidelines, their European counterpart refers to complementary characteristics of merging companies. The latter however underlines the integration of complementary activities and products, while the former emphasizes combining complementary assets, which should be understood as a slightly narrower concept of such efficiencies.[211]

Similarly to the U.S. 2023 guidelines, their EU counterpart does not devote much attention to EDM, nevertheless, they refer to it in the first place among other possible efficiencies resulting from vertical mergers. In addition, the EU NHM Guidelines mention a couple of other efficiencies, those are: better coordination of the production and distribution process, and alignment "of the incentives of the parties concerning investments in new products, new production processes, and in the marketing of products."[212] At the same time, the EU NHM Guidelines seem to consider EDM as the highly expected result of vertical concentration.[213] Still, to be considered an efficiency, the EDM must fulfill the three-element test provided in the EU Commission horizontal merger guidelines, that is, they must benefit consumers, be merger-specific, and be verifiable. As it has been held in the EU NHM Guidelines:

> The problem of double mark-ups is not always present or significant pre-merger, for instance, because the merging parties had already concluded a supply agreement with a price mechanism providing for volume discounts eliminating the mark-up. The efficiencies associated with the elimination of double mark-ups may thus not always be merger specific because vertical cooperation or vertical agreements may, short of a merger, achieve similar benefits with less anti–competitive effects. In addition, a merger may not fully eliminate the double markup when the supply of the input is limited by capacity constraints and there is an equally profitable alternative use for the input. In such circumstances, the internal use of the input entails an opportunity cost for the vertically integrated company: using more of the input internally to increase output downstream means selling less in the alternative market.

[210] *See id.* ¶ 53.

[211] *See id.* ¶ 13.

[212] *Id.* ¶ 57.

[213] *See id.* ¶ 13 ("In vertical relationships for instance, as a result of the complementarity, a decrease in mark-ups downstream *will lead* to higher demand also upstream. A part of the benefit of this increase in demand will accrue to the upstream suppliers. An integrated firm *will take* this benefit into account. Vertical integration may thus provide an increased incentive to seek to decrease prices and increase output because the integrated firm can capture a larger fraction of the benefits." (emphasis added)).

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As a result, the incentive to use the input internally and increase output downstream is less than when there is no opportunity cost.[214]

Therefore, the EU NHM Guidelines call for a prospective analysis focused on the influence of a merger on the EDM. At the same time, the EDM analysis under the U.S. 2023 Merger Guidelines seems to be more complex covering not only future elements but, inter alia, contracts existing short of a merger.[215]

The U.S. 2023 Merger Guidelines more than their EU counterpart correspond to what the results of empirical research and contemporary economic theories say about the possible effects of vertical mergers. Under both guidelines EDM is not understood as an inevitable consequence of vertical concentrations but as one of the many potential efficiencies resulting from them. Its merger specificity is rightly assessed prospectively, taking into account possible alternatives including those resulting from the relevant long-term contracts. While under the U.S. 2023 Merger Guidelines, the EDM ceased to be a "get out of jail free" card for the merging parties, it has never played this role under the EU NHM Guidelines. They provide the Commission with all the necessary tools to verify it and assess its merger specificity and the effects that the EDM may have on competition.

Although it still seems that the EU NHM Guidelines overestimate the frequency with which EDM accompanies vertical mergers and its role in counterbalancing their negative effects, they still require EDM to meet the same conditions as other efficiencies. In general, the EU concept of efficiencies as contained in the EU NHM Guidelines, though not perfect, allows for a proper and thorough analysis of their relevance in countervailing the adverse effects of vertical mergers on competition. This does not mean however that the EU NHM Guidelines do not require a refinement. First, it must be underlined that the U.S. 2023 Merger Guidelines, as opposed to its EU counterpart, rightly mention that EDM may occur only in specific circumstances. Therefore, small changes in the rhetoric of the EU NHM Guidelines may be needed to equalize the importance of EDM and other possible economic efficiencies that may arise from vertical mergers, including organizational, production, managerial, and distributional benefits as well as those related to avoidance of transaction costs. It must be remembered however that, as shown by Grossman and Hart,[216] the allocation of property rights as a result of vertical integration does not eliminate incentives for opportunistic and distortionary behavior inherent to long-term contracts existing otherwise and may as such be a source of distortions. Thus, organizational and managerial efficiencies as a result of vertical mergers are far from evident and should be reviewed with skepticism. This should be reflected in the EU guidelines.

Moreover, the U.S. 2023 Merger Guidelines rightly put more emphasis on structural concerns, including by analysis of overall trends in vertical integration in the relevant industries. This reflects a change in the perspective applied by U.S. antitrust authorities, who are now focusing more on protecting the competitive structure of increasingly concentrated markets. The EU NHM Guidelines should follow the same path by implementing a rebuttable presumption of anticompetitiveness of vertical mergers between the parties of high market shares. The threshold of 50%, suggested by the U.S. agencies seems to be at least equally appropriate for the EU competition law. First, the relevant market share of at least 50% has been considered in the well-established Court of Justice of the European Union ("CJEU") case law as a threshold for a presumption of a dominant position.[217] Linking the presumption of prohibition of concentration with the threshold of dominance is justified from the point of view of the construction of the EU

[214]*See id.* ¶ 31.

[215]*See* U.S. 2023 Merger Guidelines, *supra* note 11, at 16.

[216]Grossman & Hart, *supra* note 27, at 716.

[217]*See* ECJ, Case C-62/86, AKZO Chemie BV v. Comm'n, ECLI:EU:C:1991:286, ¶ 60, https://curia.europa.eu/juris/liste.jsf?num=C-62/86; CFI, Case T-221/95, Endemol Ent. Holding BV v. Comm'n, ECLI:EU:T:1999:85, ¶ 134, https://curia.europa.eu/juris/liste.jsf?num=T-221/95; CFI, Case T-102/96, Gencor Ltd. v. Comm'n, ECLI:EU:T:1999:65, ¶ 205, https://curia.europa.eu/juris/liste.jsf?num=T-102/96; *see also* ECJ, Case C-85/76, Hoffman-La Roche & Co. AG v. Comm'n, ECLI:EU:C:1979:36, ¶ 41, https://curia.europa.eu/juris/liste.jsf?num=C-85/76.

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SIEC test, still partly based on the concept of a dominant position. In this approach, further increasing the potential of the alleged market dominance, even by way of a vertical concentration, should be treated as a potential threat to competition. Second, establishing the presumption of prohibition based on such a threshold would be tantamount to assuming potentially equivalent anticompetitive effects of horizontal and vertical concentrations. The 50% share threshold should apply not only to the upstream and downstream markets in which the parties to the concentration operate but also to all related markets, that is, those in which a high share of the parties may contribute to the foreclosure of markets in which they operate.

This presumption should be rebuttable when a party to the concentration shows that other factors having a redeeming value are present. The most important of them should be market efficiencies fulfilling criteria similar to those provided in the current EU NHM Guidelines and refined in the way described above, that is, in a way that decreases the relevance of the EDM, organizational, and managerial efficiencies. The catalog of the redeeming factors should not be limited to possible efficiencies and cover all factors that may prove that no substantial impediment to effective competition is threatened by the merger, including the probable market entry, and failing firm argument.

The remaining concentrations should be assessed based on the theories of harm adjusted in the way presented above, that is, supplemented with the criteria of the differentiated nature of products offered in relevant markets, an overall trend to foreclose existing in a relevant or a related market, and the general purpose of the parties to foreclose the rivals as one of the arguments against the legality of mergers.

The assessment of non-horizontal mergers, according to the proposed test, could result in different outcomes in some of the most controversial cases in which the Commission issued positive decisions, including Facebook/WhatsApp Merger.[218] In this case, the share of the parties in the market concerned by the transaction—that is, the market for consumer communications services—was lower than 50%. However, it can be assumed with a high degree of probability that in 2014 Facebook, which at the time was by far the strongest player in the market, had a share in the EU market for social networking services exceeding this threshold. Since these services are complementary to consumer communication and may increase the value of rivals' products, these services match the concept of the related product. Therefore, the presumption of anticompetitiveness of this concentration would apply. Obviously, it is hard to *ex post facto* fully assess the relevance of the potential efficiencies resulting from this merger, though it is at least doubtful that they would have had the potential to rebut the presumption of negative effects of such concentration on competition. It is hard to identify any particular benefit customers could get from adding yet another consumer communication service to a platform already operating a similar service.

Admittedly, as underlined in the guidelines, these mergers do not lead directly to a concentration of market shares. However, other harms may decide about their anticompetitive nature. Research suggests that anticompetitive vertical mergers are not generally less frequent than anticompetitive horizontal mergers.

E. Conclusions

American antitrust seems to be in the middle of changes. The greater activity of the agencies, including in vertical merger cases, has been accompanied by new merger guidelines. After years of liberal and passive antitrust policy, we face a shift towards a proactive one aimed at more intensive protection of consumers against anticompetitive mergers and practices of companies, including most of all market leaders. Based on these developments, the United States is now trying to break its stagnation in vertical merger control. The new merger guidelines issued by the U.S. antitrust agencies take into account the results of the modern views of economists and empirical research.

[218]Commission Non-opposition to a notified concentration (Case M.7217 — Facebook/WhatsApp), 2014 O.J. (C 417).

https://doi.org/10.1017/glj.2024.44 Published online by Cambridge University Press

The guidelines take broad account of structural factors, assuming that non-horizontal mergers by firms with large foreclosure shares shall generally be prohibited unless there are additional factors that undermine or offset their anticompetitive nature. They are based on an assumption that vertical concentrations can harm competition just as much as horizontal ones, as evidenced by the adoption of a uniform standard of assessment of the possibility of foreclosure for all types of mergers. At the same time, the new U.S. guidelines are skeptical about the frequency of EDM resulting from vertical mergers, expressing the view that it is possible only in specific circumstances.

After many years of the intellectual influence of the American antitrust on global and EU competition law, in the last dozen or so years, the EU competition policy, as more active, seemed to set the tone in the battle against anticompetitive practices and concentrations. The new U.S. 2023 Merger Guidelines can be assessed in various ways. It is clear, however, that more than their EU counterpart, they take into account modern economic theories and current economic reality dominated by the ongoing processes of vertical market consolidation. In this context, new U.S. developments analyzed above mean that the American antitrust law, at least in the area of non-horizontal mergers, has jumped over the back of its EU counterpart and moved to the forefront. Of course, the condition for the success of these changes is their support by the federal judiciary, which has not happened yet. The future of the U.S. approach to vertical mergers is thus still unclear.

Nevertheless, in this leapfrog game, where the EU keeps jumping over the U.S.'s back and vice versa, the European Union should not be lagging. The revision of the EU NHM Guidelines seems needed so that the U.S. back does not have to be viewed.

Acknowledgements. I would like to express my profound gratitude to Professor Spencer Weber Waller for all his exceptional support and guidance provided for me during my work on this contribution and to Professor Imelda Maher for all her invaluable comments and suggestions.

Competing Interests. The author declares none.

Funding Statement. This work has been financed by the Polish National Agency for Academic Exchange in the framework of the research project "Application of the Competition Law to non-horizontal mergers in the Digital Era. A comparative study" ("Stosowanie prawa konkurencji do niehoryzontalnych koncentracji przedsiębiorców w epoce cyfrowej. Analiza porównawcza") under the M. Bekker Programme.

Cite this article: Grzejdziak Ł (2024). U.S. and EU Non-Horizontal Merger Guidelines: A Friendly Game of Leapfrog. *German Law Journal*, 1–31. https://doi.org/10.1017/glj.2024.44

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