One-and-a-Half Cheers for the New FTC Remedies Study

The Federal Trade Commission has released its study of its remedy orders between 2006 and 2012. Notice of this study was issued in early 2015, so the process has taken two full years to bring to completion. I think the FTC deserves much credit for undertaking this study. Agencies do not often review the effects and effectiveness of their past policies and practices. It takes time and resources from current activities, and then the results may not be favorable to the agency, posing risks of criticism and worse. So it is a sign of good government when an agency does this. Kudos to the FTC.

This is the second such study done by the FTC. The first, in 1999, was widely recognized as a milestone and resulted in a number of significant changes in the Commission's divestiture policy. It has now been replicated in a number of other countries that have also assessed their remedies practices. This new FTC study has a number of notable features. It covers many more remedies than the earlier one, and obviously focuses on more recent experiences. The involvement of the Bureau of Economics undoubtedly strengthened the analytic foundations of the work. It forthrightly reports a less than perfect record for some of its remedies. And it uses its review to identify ways of improving remedy policy going forward. This, too, is all much to the credit of the agency.

That said, I find that this study is ultimately uneven. While in some places its methodology and conclusions represent advances over its earlier study, in many places it does no better than before, and occasionally even worse. This is greatly disappointing. With growing emphasis on remedies, with advances in methods of analyzing policy, and with many comments and suggestions to the FTC in this proceeding, this study was an opportunity to substantially advance our understanding. Instead, it mostly offers some incremental insights.

In the rest of this commentary, I elaborate on my mixed assessment of the FTC Report, first with respect to its methodology and then its conclusions.

A. Methodology of the FTC Report


3 This study lists 115 people as having contributed in some fashion to the study and the report.


5 For a listing and review of these other studies, see my book, Mergers, Merger Control, and Remedies, MIT Press, 2015, ch. 8. There also were some weaknesses to the 1999 study, which I discuss below.
(1) To begin, the scope of this study was intended to be broader than the 1999 study. The earlier study examined only divestitures, whereas this new study set out to include conduct remedies as well. Even among the 89 orders covering seven years, this study found too few of the latter to draw any conclusions. That is, of course, hardly the agency’s fault, but quite unfortunate since conduct remedies are widely believed to be more frequent in the past ten to fifteen years and have become quite controversial. It is not clear how long a period would have been necessary to find a sufficient number of observations, but this is a significant lost opportunity to inform policy about these remedies.

(2) This study inexplicably uses three quite different methodologies for assessing the outcomes of the 89 total orders. For 50 orders (56% of the cases), the procedure involved full blown case studies, similar (but not identical, for reasons below) to the 1999 study. For the other 39 orders, no case studies were done at all, but instead the FTC used only considerably less complete information. Of those 39, 15 orders were assessed based simply on questionnaires to outside parties, while the remaining 24 (27 percent) orders--all in the pharmaceutical industry--were assessed based on nothing more than the FTC’s own records of their past actions and monitoring of the markets.

I said this was “inexplicable,” but in fact the FTC did offer a rationale for this differential treatment. In the original notice for this study, the FTC declared that, with respect to the questionnaire-based assessments, it had “extensive expertise in crafting remedies for mergers in certain industries,” and that for the records-based assessments in the pharma sector “staff has a great deal of information” on divestitures as well as “close contact with the monitors appointed in the majority of these orders.” From this, the FTC concluded that interviews were unnecessary.

It is difficult to be satisfied with the questionnaire procedure, and impossible to be satisfied with the internal records-based assessment procedure. Questionnaires tend to produce formal declarative responses without the subtleties of interviews. They are not well suited to follow-up questions tailored to the circumstances. Records-based assessments are informational closed loops: whatever the agency records and personnel do not know will remain unknown to those who rely on them. Neither of these techniques–certainly not the internal records-based assessments--is a satisfactory basis for the agency’s determinations.

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6 FTC Notice, p. 2424.

7 Ibid.
When the FTC outlined this tripartite methodology in the original Notice, I submitted comments that pointed out these concerns and urged instead a consistent and thorough methodology for assessing all the orders.\(^8\)  I have no doubt that the costs of doing 89 rather than 50 full blown case studies are nontrivial.  On the other hand, to undertake this study and fail to do the necessary analysis on nearly half of the orders is unfortunate, to say the least--truly a missed opportunity.  Worse yet, by failing to use a consistent methodology, the results are not equally strong and certainly not comparable across all subsets of the cases.  As a result, as I said, my view is that this study is very uneven.

(3) In addition to different methodologies, the FTC Report uses different criteria for what it concludes to be a "successful" order across these different categories.  For those 50 fully assessed orders, the Report describes the test as whether competition “remained at its premerger level or returned to that level within...two to three years.”  By contrast, for the 15 orders assessed using questionnaires, "success" is defined simply as continued production of the divested product, not whether competition was preserved or restored by the remedy.  For the remaining 24 orders arising in the pharmaceutical industry, the criteria for “success” vary even further.  For orders addressing cases where both merging parties sold the product, “success” is again defined as continued production of the product.  But for cases of divestiture of “pipeline products”--those in the development stage--the divestiture was viewed as successful simply if the assets designated for transfer were in fact transferred.  This does not even purport to measure survivorship of the assets for any period of time, much less their competitive effects.

A bit of history is useful here.  The FTC’s 1999 Divestiture Study assessed remedies strictly by whether the divested assets remained in the industry in the postmerger, post-remedy period.  But this criterion--essentially asset viability--is a necessary but not sufficient condition for the preservation or restoration of competition.  They certainly should not be viewed interchangeably.\(^9\)  So while the FTC improved on its earlier practice and adopted the correct standard for a successful remedy for the 50 case studies, it has persisted in using this incorrect standard (or an even weaker one) to assess the remaining 39 orders.  It compounds this error by using this same term--"success"--to describe all of these varied outcomes, even though only one is correct.  This certainly improves the apparent "success" rate of its remedies, but equally certainly it invites misinterpretation.

(4) Even with the 50 orders assessed with case studies, the criterion for “success"


\(^9\) Language to that effect can be found in the FTC's own Statement on Negotiating Merger Remedies (2003), in the DOJ's Policy Guide to Merger Remedies (2004, 2011), and indeed in this Report (p. 1).  This Report calls it a “high bar,” but any lower bar would not be the correct standard.  I pointed out these issues in my original comments in this proceeding, and urged the FTC to adopt the correct standard throughout.  Kwoka, “Comments."
deserves comment. Without explanation, a two to three year delay in restoration of competition is viewed as a fully successful remedy, even though much harm may occur in such an interval. Relative to doing nothing, that may seem the better course, but relative to prohibiting the merger altogether, that period represents a true loss of some magnitude.

The Report declares a remedy to be a “qualified success” if competition is restored but it takes more time than two or three years. But if competition returns in more than three years, it could easily be due to exogenous factors or to endogenous responses within the market—neither of which should be credited to the remedy. This is especially true since the criterion of “more than two or three years” can mean any number of years after the remedy is imposed. For this reason, I recommend that the agency report more fully on the time period required for a return of competition to those cases it termed “qualified success.”

And finally, the Report describes some of the factors and evidence that went into its determinations of successful remedies. These are all familiar to an economist’s assessment, but the process is still pretty opaque. While there is no way that all of the evidence could be put on the public record, there is one important action that the FTC still can and should do to improve transparency. For these 50 fully analyzed orders, the FTC should now release its “scorecard” indicating which ones it judged to be successful and which not. This would not violate confidentiality, but it would help make its conclusions more convincing.10

B. Conclusions of the FTC Report

Some of the conclusions of the FTC Report are bit scattered, so it may be useful to pull them together in summary form. First, for the 50 orders assessed with full case studies and employing the criterion of competition, the FTC reports full “success” in about two-thirds of cases involving horizontal concerns. By adding the cases of “qualified [that is, delayed] success,” the Report states that “with respect to the orders examined [more precisely, of this category of orders], more than 80% of the Commission’s orders maintained or restored competition.”11 The Report goes on to analyze various details and implications of these 50 case studies in 18 pages.

Oddly, in contrast, the Report devotes a single page to its conclusions with respect to the 15 orders assessed using questionnaires. This may be a reflection of the minimal depth of this method of analysis. Recalling that these were judged “successes” against the lower bar of continued production, the Report states that 39 of a total of 43 products covered by these 15 orders were “successes,” which implies a 91 percent “success” rate. The Report does not address

10 Along the same lines, to improve transparency and credibility where an agency conducts a retrospective on its own actions, I have recommended that there be an independent outside monitor who can inspect the data, query the analysis, and ultimately attest that the agency’s conclusions are fundamentally sound.

11 Report, p. 2.
the fraction that preserved or restored otherwise lost competition.

The conclusions for the remaining 24 orders are also discussed in a single page in the Report. These orders covered 92 cases in pharmaceuticals, divided as follows: Of 60 cases of product overlaps between the merging companies, 18 cases involved contract manufacturing, so that all that was required was re-assignment of the supply agreement. All of these 18 contracts were in fact re-assigned, leading the Report to declare them “successes.” Another 42 product overlap cases involved the need for divesting manufacturing assets. Of these, there were 27 “successful” asset transfers and 15 failures. Finally, all of the 32 cases involving divestiture of product development assets were declared “successes” by virtue of the fact that the transfers in fact occurred, regardless of what ensued. For none of these do we learn anything about the fraction of orders that resulted in the preservation or restoration of competition.

I now offer some observations on these conclusions and additional recommendations.

(1) The report highlights the rate of success for the 50 orders assessed using case studies. Among the 46 horizontal cases, 66 percent were fully successful (69 percent of all cases in this category). Read differently, however, that implies that in one-third of cases, competition was lost for a minimum of two or three years and perhaps indefinitely. One obvious question is whether this is an acceptable failure rate—that is, whether it satisfies the objective of remedies, or whether it signals the need for more outright enforcement actions against such mergers. Views on this will differ, but I do not think that competition denied or significantly postponed in one-third of cases is a basis to conclude that remedy policy is truly doing its job.

(2) I think the FTC can and now should further exploit the data and investigate the roots of success or failure of these 50 remedies. Having judged which were successfully resolved, the next step should be to conduct a statistical analysis of the factors associated with different outcomes. These factors might involve characteristics of the product, the market, the firms, the transaction, and the specific competition problem. That would permit answering such questions as whether the rate of success varies with the size of the firms, or with the heterogeneity of the products, and so forth. A further analysis along these lines could significantly advance understanding of when and where remedies should be used, and when and where they should not, at least not in their present form—important questions that can be examined without the need for much if any new data collection, and certainly not another study.

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12 There is some discussion of this in various places in the Report, but that does not qualify as statistical analysis.
(3) The FTC Report found a substantially lower rate of success—about 56 percent of orders—where a divestiture remedy transferred less than the entirety of a business unit. As a result, it stated its “preference” for divestitures of entire business units.\(^\text{13}\) This finding is no surprise, however, since the 1999 Study found only a 60 percent “success” rate measured against the lower bar of asset viability for these kinds of divestitures. That earlier report also recommended against them for that reason.\(^\text{14}\) But having already studied these partial-entity divestitures and determined them often to be failures, the obvious question is why the FTC has not followed its own advice but instead persisted in pursuing a flawed strategy. In this Report the FTC asserts that it resorts to partial-entity divestitures only when necessary, but that would seem to mean “when necessary to use some kind of remedy instead of challenging the merger.” But it is not necessary to use a remedy. Such a high rate of failure—nearly half the time—signals instances in which stricter enforcement is called for. I think the FTC should now face a far heavier burden for resorting to such remedies in the future.

(4) For the other 44 percent of non-case-study orders, the FTC Report simply errs in lowering the standard for “success.” It is only by declaring a remedy “successful” if a contract or project that was required to be transferred was in fact transferred, that the Report arrives at a 100 percent “success” rate for such remedies. In more challenging cases where physical assets needed to be transferred, 64 percent resulted in “successful” transfer, but in each case, the true percent of cases that preserve or restore competition is strictly lower. I have already noted that this low standard is substantively incorrect, and the use of the same terminology invites an exaggerated view of success of remedy policy.

Finally, I commend the FTC for its “Best Practices” section, which is devoted to extracting lessons from its analysis of remedial orders. While I think some stronger conclusions might have been warranted, this is an enormously valuable part of what the FTC has done.

**My Recommendations**

As I said, the FTC deserves much credit for putting itself under a microscope and acknowledging some instances in which its policies have not worked. But as I also said, and now have detailed, the study is uneven and sometimes flawed in its methodology, and for that reason it ultimately fails to deliver on its considerable promise. There are, however, a number of actions that the FTC can still undertake that will advance understanding about the effects and effectiveness of its remedy policies.

First and foremost, the FTC should complete its job. It should immediately return to the 39 orders where it relied on questionnaires and internal reports and undertake the necessary full case studies. Also for these 39 orders, it should evaluate the success of the remedy by the correct standard of whether it preserved or restored the competition lost due to the merger—and

\(^\text{13}\) Report, pp. 22, 32.

\(^\text{14}\) FTC Divestiture Study, pp. 11-12
only use the term “success” for this standard. This further work will take full advantage of what has already been done. It will ask and answer the right question about remedies. And it will not require waiting another 18 years to learn the answers.

Apart from that, there are other ways in which the FTC can exploit the data it already has compiled. In this commentary, I have recommended the following extensions of this FTC study:

(1) The FTC should report data on the delays it observed in restoring competition for those remedies that did not do so immediately. For those described as “successes,” it would be useful to know how many took fully three years, for example, and for those with greater delays (“qualified successes”), what were the frequencies of long delays (e.g., 5 or more years).

(2) The FTC should release a scorecard of the 50 orders assessed with case studies, with an indication of those that were full “successes” vs. “qualified [delayed] successes” vs. “failures.”

(3) The FTC should compile further information on the firm, market, and product characteristics associated with the 50 orders and conduct a statistical analysis of the correlates of success vs. failure. The results of the analysis should be made public.

Furthermore, going forward, I would recommend the following:

(1) The FTC should not be using divestitures of less than entire business units. The two FTC studies have demonstrated that this approach did not work before and has continued not to work in a large fraction of cases. The lesson needs finally to be learned: if a merger cannot be remedied, it should be challenged.

(2) The FTC should redouble its efforts to compile data and other information on conduct remedies. While fewer in number than those for the horizontal mergers focused on in this Report, conduct remedies have been used in a variety of antitrust contexts where their effectiveness has been questioned.

(3) And finally, rather than conducting retrospectives on batches of remedies many years later, as the 1999 study and this study have done, the FTC (and yes, DOJ!) should compile data and conduct assessments of their remedy experiences on an on-going basis. Continuous study and learning will provide further insights as to how policy has been working and can be improved on an on-going basis. And these new studies should henceforth only be evaluated against the correct standard of preservation or restoration of otherwise lost competition.

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