



ILLUMINA/GRAIL: FTC ILLUMINATES THE PATH OF FUTURE VERTICAL MERGER REVIEW

by Gerald A. Stein and Marisa Madaras

As the U.S. antitrust bar anxiously awaits the release of the federal agencies' revised merger guidelines, the Federal Trade Commission's Illumina/Grail opinion and order (the Opinion) offers the most recent and comprehensive indication of how the Commission will approach vertical merger transactions and proposed remedies. Such treatment has been an object of speculation since the FTC withdrew the 2020 Vertical Merger Guidelines in September 2021.

Illumina, Inc., a DNA sequencing company, acquired GRAIL, Inc., a healthcare company that makes a multi-cancer early detection (MCED) test.¹ Illumina produces next-generation sequencing (NGS) platforms, which are key inputs for MCED testing. Illumina created GRAIL in 2015 and spun it off two years later, maintaining a minority interest in GRAIL until agreeing in 2020 to purchase back the remaining shares. In ordering Illumina to divest GRAIL, the FTC found that the \$8 billion acquisition may incentivize Illumina to favor GRAIL over other MCED test producers in its provision of NGS inputs. The possibility of preferential treatment, the FTC reasoned, could harm competition in the research and development of MCED tests. The unanimous Opinion issued by the full Commission reversed the November 2021 initial decision of the FTC's administrative law judge (ALJ) that had dismissed an FTC staff complaint filed in March 2021. The parties have appealed the decision to the U.S. Court of Appeals for the Fifth Circuit.

Perhaps the most noteworthy aspects of the Opinion are the two sections highlighted by then-Commissioner Wilson in her concurring opinion:² (1) The FTC's use of both the *Brown Shoe* standard and the ability-and-incentive framework in evaluating the anticompetitive effects of the transaction; and (2) the Commission's treatment of the contractual agreements between Illumina and customers that would prevent Illumina's foreclosure of GRAIL's competitors ("the Open Offer").

The *Brown Shoe* Standard

In evaluating the anticompetitive effects of the vertical merger, the FTC applied two "different but overlapping standards":³

¹ Opinion of the Commission, *In re Illumina, Inc., and GRAIL, Inc.*, Docket No. 9401 (FTC Mar. 31, 2023), available at Illumina/Grail: Final Commission Opinion (ftc.gov); Final Order, *In re Illumina, Inc., and GRAIL, Inc.*, Docket No. 9401 (FTC Mar. 31, 2023), available at Illumina/Grail: Final Order (ftc.gov).

² Concurring Opinion of Commissioner Christine S. Wilson, *In re Illumina, Inc., and GRAIL, Inc.*, Docket No. 9401 (FTC Mar. 31, 2023), available at Illumina/Grail: Concurring Opinion of Commissioner Christine S. Wilson (ftc.gov).

³ Opinion of the Commission at 40.

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- (1) The *Brown Shoe* standard under which the FTC examined factors identified by *Brown Shoe* and its progeny including the nature and purpose of the transaction, the likely foreclosure of competition by one of the merging parties, entry barrier, and the degree of market power that would be possessed by the merged firm.
- (2) The “Ability and Incentive” Framework which focuses on whether the transaction will increase the ability and heighten the incentive of the merged firm to foreclose rivals’ access to sources of supply or outlets for distribution.

Despite holding that the ALJ erred in requiring a showing of harm under both *Brown Shoe* and the ability and incentive framework, the FTC examined the transaction under both standards “for the sake of completeness” and concluded that, under either standard, the FTC established a *prima facie* case of the anticompetitive effects of the acquisition.⁴ Accordingly, the FTC held that the acquisition violated Section 7 of the Clayton Act and Section 5 of the FTC Act.

In her concurring opinion, Commissioner Wilson disagreed with the FTC’s use of the *Brown Shoe* standard to establish a *prima facie* case, stating that there is no *Brown Shoe* standard in modern vertical transaction antitrust analysis. In doing so, Commissioner Wilson cited the 2020 Vertical Merger Guidelines, noting that these guidelines were withdrawn by the FTC but remain intact at the Department of Justice. The guidelines and modern case law, she wrote, only provide for use of the ability-and-incentive framework in analyzing vertical mergers. This distinction is important because, as highlighted by Commissioner Wilson, the first *Brown Shoe* factor discusses, “the share of the market foreclosed,” and therefore paints a simplistic view of the role of market share for vertical mergers that is inconsistent with modern economics and precedent. Ultimately, however, Commissioner Wilson concurred that complaint counsel did establish a *prima facie* case that the transaction was likely to lessen competition.

The Open Offer

The Open Offer consisted of terms that included, *inter alia*, a 12-year supply agreement under which Illumina would commit not to increase the price of sequencing instruments or consumables; would commit to decrease the cost of sequencing on Illumina’s highest-throughput instrument (using the highest-throughput consumable); and would commit to provide access to the same sequencing products at the same pricing provided to GRAIL. Relying on the terms of the Open Offer, the ALJ found that the FTC had failed to show in its *prima facie* case that a likelihood of harm to GRAIL’s rivals is “probable or imminent,” and consequently, he found, the FTC could not demonstrate that a resulting substantial lessening of competition is probable or imminent. On appeal, however, the Commission found that the Open Offer constituted a proposed remedy and, overturning the ALJ’s findings, found that as a proposed remedy (as opposed to an existing economic market condition) it was the parties’ burden—not the FTC’s—to prove that the Open Offer would overcome the anticompetitive effects of the merger and that the parties failed to do so.

While agreeing that “even after considering the effects of the Open Offer, anticompetitive effects are likely and the transaction is likely to lessen competition substantially,” Commissioner Wilson disagreed with the FTC’s treatment of the Open Offer as a proposed remedy considered only after a finding of liability.⁵ Commissioner Wilson opined that the Open Offer should be considered part of Respondents’ rebuttal in the analysis of the merger’s competitive effects. She distinguished cases cited by the Opinion in which similar terms were conditional on the deal closing by pointing out that the Open Offer had already been incorporated into some of Illumina’s contracts, making it

⁴ *Id.* at 41.

⁵ Concurring Opinion of Commissioner Christine S. Wilson at 5.

a market reality that the FTC should consider its finding of liability.

This Opinion is a significant guidepost for the FTC's approach to vertical merger transactions and may provide some preview to the much-awaited revised merger guidelines. The Opinion offers insight to how the FTC might evaluate the competitive effects of a vertical merger and remains in step with the FTC's recent practice of reviving seemingly dormant case law. In addition, the FTC's treatment of the Open Offer as a proposed remedy and not a market condition shows how the Commission will consider the merging parties' efforts to overcome potential anticompetitive effects. However, with many questions still unanswered and an appeal pending, the FTC's approach to vertical mergers remains a space to monitor.