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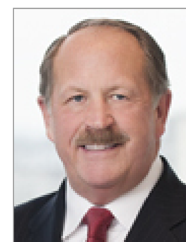
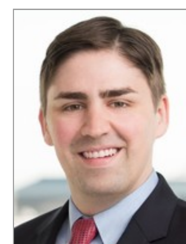
What To Expect From FTC's Big Tech Merger Review

By **Raymond Jacobsen and Jonathan Ende** (April 27, 2020, 5:22 PM EDT)


Raymond Jacobsen


Jonathan Ende

On Feb. 11, the Federal Trade Commission announced that it had issued special orders to five large technology companies, requesting information on prior acquisitions completed by the companies during the past 10 years.

The FTC's announcement follows several recent high-profile events relating to technology mergers, including the FTC's Hearings on Competition and Consumer Protection in the 21st Century and the FTC's creation of a Technology Task Force.[1] The continuing timeliness of the special orders was made evident by recent remarks from FTC Commissioner Christine Wilson. According to a podcast released for the American Bar Association Antitrust Section's Virtual Spring Meeting ("Merger Analysis Gone Digital: Time to Reboot?"), Commissioner Wilson reportedly said that the public should expect to see more challenges of mergers that threaten to eliminate potential competition.

The five companies subject to the special orders are Alphabet Inc. (which includes Google Inc.), Amazon.com Inc., Apple Inc., Facebook Inc. and Microsoft Corp. The special orders request information and documents on corporate acquisition strategies, purposes of the prior deals, post-acquisition product development and pricing, and other agreements relating to the deals.

The FTC's investigation focuses on transactions that were not reportable to the FTC or the Antitrust Division of the U.S. Department of Justice under the Hart-Scott-Rodino Act.

For the most part, transactions are not reportable under the HSR Act if they fall below the size-of-transaction monetary threshold. During the period covered by the special orders, the HSR size-of-transaction threshold, which adjusts annually based on growth of the GDP, started at $63.4 million in 2010 and grew to $90 million in 2019. Therefore, the deals subject to the special orders were relatively small transactions, and many likely involved the acquisition of potential or nascent competitors, firms that have yet to or are in the early stages of entering and competing in a market.[2]

The key question driving the FTC's special orders is whether nonreportable deals might warrant further investigation or challenge. The special orders present challenges and opportunities for the five companies and for other acquisitive companies that may face questions down the road.

The Five Subject Companies Have Been Acquisitive

All five of the companies subject to the special orders have been active in making acquisitions during the period covered by the special orders. Based upon publicly available information, the five companies collectively made upwards of 550 acquisitions during the 10-year period, well over 100 of which were likely nonreportable under the HSR Act.

Of the hundreds of acquisitions made by the companies, only one HSR-reportable transaction appears to have been challenged by the FTC or DOJ: Google's 2011 acquisition of ITA Software Inc.

The DOJ's challenge resulted in a consent decree that required Google to continue to honor ITA Software's existing software licenses and offer new licenses on fair, reasonable and nondiscriminatory terms; to devote resources to research and development similar to what ITA Software had devoted before the acquisition; to implement firewalls to ensure the confidentiality of information belonging to ITA Software customers; and to report certain complaints that Google has treated ITA Software's customers unfairly.[3]

Nonreportable Acquisitions by These Companies May Be Difficult to Challenge

One major question is whether the FTC might retroactively challenge one or more of the acquisitions it is investigating — seeking a potential divestiture or behavioral remedy. Such an outcome would have difficulties. The FTC is still bound by the merger guidelines.

Under the merger guidelines, the FTC would need to show generally that one of the reviewed deals raised unilateral or coordinated concerns in a properly defined market. The FTC might face difficulties for several reasons.

Frequently, in acquisitions by big tech companies, the acquiring company and the target company are not close competitors to each other or operate in distinct markets. Several deals involving big tech companies that exemplify this were Google's acquisition of DoubleClick, Facebook's acquisition of WhatsApp Inc., Amazon's acquisition of Whole Foods Market Inc., and Apple's acquisition of Shazam.

In the Google/DoubleClick deal, the FTC publicly acknowledged that the merging parties were not direct competitors.[4] Panelists participating in the FTC's Hearings on Competition and Consumer Protection in the 21st Century described several additional features of nascent acquisitions in technology markets that make the transactions difficult to challenge. The panelists explained that acquisitions of nascent competitors by larger, more stable firms are often pro-competitive because of the rate of failure of technology startups.

In addition, the antitrust agency may have a difficult time proving that the nascent competitor would have been able to timely enter and grow, which is a requirement under the merger guidelines. This may be particularly difficult in technology markets that are tilted toward incumbents because of network effects.

Other features of technology markets, such as dynamism, zero-price services, and presence of platform firms may make determination of unilateral or coordinated effects challenging. While Commissioner Wilson indicated in her recent remarks that more transactions involving potential or nascent competition will be challenged, she also acknowledged that some difficulties will be presented.

Companies Need to Be Prepared to Explain Any Questionable Post-Acquisition Conduct

Despite the obstacles that the FTC faces in challenging nascent acquisitions, companies need to be sensitive to their conduct after closing an acquisition. The FTC specifically requested information on post-acquisition product development and pricing in the special orders. Evidence of post-closing price increases or a decrease in product development may make it easier for the antitrust agencies to establish anti-competitive effects of an acquisition of a nascent competitor.

There are several forms of post-acquisition conduct by the acquiring company that could raise competitive concerns.

One form is failing to develop the nascent firm's technology. A panel at the Hearings on Competition and Consumer Protection in the 21st Century explained that, in some nascent technology acquisitions, the greatest competitive harm may be caused by decreased innovation.

A second form is foreclosing access to the nascent firm's technology. The DOJ raised this concern when it challenged Google's acquisition of ITA Software, and several of the remedies imposed in the DOJ's consent decree were designed to prevent foreclosure.

A third form is significantly raising prices on the nascent firm's technology following the acquisition. Price increases may occur after any merger, but there may be greater ability to raise prices after a nascent technology acquisition because the products and services developed by technology startups are often unique.

The respondents to the special orders, as well as other technology companies that make frequent acquisitions, should be prepared to offer pro-competitive rationales for post-acquisition conduct. In particular, companies should have explanations prepared for any of the forms of conduct described above: any failure to develop the target firm's technology; any foreclosure of the target firm's technology to other firms; or any significant price increases following the acquisition.

Rationales should be supported by concrete proof, such as ordinary course documents and economic data.

Special Report Could Be Precursor to Other FTC Investigations

While the FTC's current focus is on the big tech companies, similar investigations may follow in other industries. Two FTC commissioners, Christine Wilson and Rohit Chopra, wrote a statement in support of the special orders.[5] In their statement, the commissioners called for the FTC to analyze nonreportable deals in the health care industry.

Panelists at the Hearings on Competition and Consumer Protection in the 21st Century questioned whether there is too much market concentration across the economy. These kinds of conversations may encourage the FTC to pursue investigations in other industries.

Therefore, any large, acquisitive company should be prepared to defend HSR nonreportable deals, even after the deal has been completed. Companies should be cautious about the content of internal documents and rationales for deals, pre- and post-acquisition, because such documents may be reviewed later by an antitrust agency.

Post-acquisition conduct involving the target firm's business should be reviewed and vetted, particularly if there is a possible perception of anti-competitive intent or effect. Decisions to raise prices, discontinue product development or research, change licensing or distribution practices, or enter into exclusive arrangements should all be approached judiciously.

More than 50 years ago, the U.S. Supreme Court recognized in U.S. v. E.I. du Pont de Nemours & Co. that divestitures can be sought of consummated transactions.[6] The power of the antitrust agencies to challenge consummated transactions was reaffirmed a little more than a decade ago by the FTC in In re: Evanston Northwestern Healthcare Corp.[7]

Counsel for acquisitive companies should be alert to avoiding conduct in consummated transactions that may raise anti-competitive issues, and be prepared to explain and defend any such conduct.

Raymond Jacobsen is a partner and Jonathan Ende is an associate at McDermott Will & Emery LLP.

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[1] Raymond Jacobsen et al., FTC Task Force May Lead to Wider Enforcement in Tech, Law360, (Mar. 6, 2019), https://www.law360.com/articles/1135626/ftc-task-force-may-lead-to-wider-enforcement-in-tech.

[2] A nascent competitor is a firm that currently operates in a market but is not a mature or significant competitor yet. A potential competitor is a firm that does not currently compete in a market but is expected to compete at some point in the future. Because nascent competitors and potential competitors are not standard market participants, antitrust law has developed separate doctrines to address conduct or mergers that harm potential competition or nascent competition.

[3] Competitive Impact Statement, United States v. Google Inc. and ITA Software, Inc., No. 1:11-cv-00688, 3 (D.D.C. Apr. 8, 2011).

[4] In re Google/DoubleClick, FTC File No. 071-0170, Statement of Fed. Trade Comm'n, at 7 (Dec. 20, 2007), https://www.ftc.gov/system/files/documents/public_statements/418081/071220googledc-commstmt.pdf.

[5] Statement of Christine S. Wilson, Joined by Commissioner Rohit Chopra, Concerning Non-Reportable Hart-Scott-Rodino Act Filing 6(b) Orders (Feb. 11, 2020), https://www.ftc.gov/system/files/documents/public_statements/1566385/statement_by_commissioners_wilson_and_chopra_re_hsr_6b.pdf.

[6] See generally United States v. E.I. du Pont de Nemours & Co. , 366 U.S. 316 (1961).

[7] See generally In re Evanston Northwestern Healthcare Corp., FTC File No. 9315, Opinion of the Commission on Remedy (Apr. 28, 2008), https://www.ftc.gov/sites/default/files/documents/cases/2008/04/080428commopiniononremedy.pdf.

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