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Bazaarvoice Shows Courts' and Agencies' Orthodox Approach to Mergers in High-Tech Markets

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The District Court's decision finding the *Bazaarvoice/PowerReviews* acquisition unlawful demonstrates that agencies and courts will continue to apply traditional methods of merger analysis based on market definition and market concentration even when customers have not opposed the transaction and the overlapping revenues involved appear to be small. The Court rejected claims that Google, Amazon, Facebook and other e-Commerce giants were competitive constraints and placed particular weight on the parties' internal documents, once again showing how difficult it can be for merging parties to impeach their own unhelpful documents.

Factual Background and Prior History

On Wednesday, the US District Court for the Northern District of California found that Bazaarvoice's June 12, 2012 acquisition of PowerReviews violated Section 7 of the Clayton Act, which prohibits any merger that may substantially lessen competition. Prior to the acquisition, Bazaarvoice and PowerReviews had been the two leaders in the US for "Ratings and Reviews" ("R&R") software and services, which allow product manufacturers and Internet retailers to solicit, moderate and display customer feedback at the online "point of sale." The elimination of PowerReviews, the District Court found, had left Bazaarvoice as an effective monopolist, with results likely to cause lasting harm to consumers in terms of both price and innovation.

Bazaarvoice's purchase of PowerReviews was not reportable under the Hart-Scott-Rodino Act, because PowerReviews' revenues fell under the Act's then applicable $13.6 million "size of person" threshold. The DOJ nonetheless opened an antitrust investigation within two days of the acquisition closing and filed suit seven months later, in January 2013. Both the

DOJ's complaint and the District Court's opinion drew heavily on internal statements made by Bazaarvoice and PowerReviews employees and executives, in which the employees characterized the R&R market as a "duopoly"[1] and PowerReviews as Bazaarvoice's "only meaningful competitor".[2] Additionally, the economic testimony presented by the government at trial led the District Court to view the R&R sector as "highly concentrated," with high barriers to entry and no meaningful countervailing efficiencies resulting from the PowerReviews acquisition.[3]

During a three-week trial, the District Court heard from more than 40 witnesses and 100 deponents. Interestingly, the testimony offered by Bazaarvoice's customers was largely neutral or positive, with none of the more than 100 current, former or potential Bazaarvoice customers testifying that the acquisition had or would harm them.[4] The District Court, however, gave these views short shrift, stating that customers "lacked the same information about the merger presented in court, including from the economic experts" and concluding that their views were "speculative at best and...entitled to virtually no weight."[5]

The case will now proceed to the remedies phase.

The District Court Engaged in an Orthodox Analysis Based on Market Definition and Concentration

While the transaction took place in a fast-moving e-Commerce market, the District Court rejected arguments that different standards should apply in high-tech, dynamic markets and engaged in an orthodox antitrust analysis of the transaction. The District Court found a relevant market, backed up by numerous internal transaction and ordinary course documents, in which Bazaarvoice's share exceeded 50%, thereby establishing a presumption of illegality. Bazaarvoice could not rebut this presumption because it could not establish sufficient ease of entry, actual entry, potential entry or merger-specific efficiencies.

While the District Court did list some economic evidence presented by the DOJ's expert, Dr. Carl Shapiro, showing that prices might increase post-merger for some set of customers, the District Court seemed to be most persuaded by the high concentration in the R&R market and the view of competition reflected in the parties' ordinary course business documents. The opinion is striking for its frequent citations to the 1992 Horizontal Merger Guidelines and its reliance on market definition, HHIs, and other structural indicators of market power. Indeed, read in conjunction with the last successful DOJ merger litigation (the 2011 *H&R Block/Tax-Act* case),[6] it appears that the agencies and the courts continue to hew to a "traditional" 1992 Guidelines approach, notwithstanding the introduction of the 2010 Guidelines.

Small, Non-Reportable Transactions are not Immune from Agency Scrutiny

This case is yet another demonstration that the antitrust agencies will investigate and bring suit to block non-reportable transactions, even after transactions have closed. Not only was the deal below the HSR thresholds, the amount of directly overlapping revenue appeared to be small, as PowerReviews generated only $11.5 million in revenue in 2011.

[1] United States v. Bazaarvoice, Inc., Memorandum Op. at 44, No. 13-00133 (N.D. Cal. Jan. 8, 2014).

[2] *Id*. at 27.

[3] *Id*. at 73, 118, 123.

[4] *Id*. at 116.

[5] *Id*.

[6] United States v. H&R Block, 833 F. Supp. 2d 36 (D.D.C. 2011).

Furthermore, a portion of PowerReviews' revenue was derived from a turn-key R&R solution that did not compete with the Bazaarvoice platform.[7] The District Court also noted that PowerReviews tended to focus on small- and medium-sized businesses while Bazaarvoice served larger retailers and brands. While it is not clear from the decision how much overlapping revenue was at issue, the amount of PowerReviews' directly overlapping revenue appears to have been under $10 million.

The District Court Discounted Customer's Views about the Transaction's Effects

While the District Court found that customers were reliable sources of information about the scope of the relevant product market and past responses to price increases, somewhat remarkably, the District Court dismissed customer testimony about competitive effects, finding that customers were not well-placed to predict the effects of a merger, especially where the products at issue are "relatively inexpensive in comparison to a company's operating budget".[8] The Court's outright dismissal of customer views on competitive effects is troubling and is likely to become a major point in any appeal.

If *Bazaarvoice* is to be a guide in problematic transactions, the merging parties need to do much more than show that customers are not opposed to the transaction. To be effective, parties are advised to produce (1) a broadly representative set of customers that show strong support for the transaction; (2) evidence that the transaction will benefit customers in some tangible way; and (3) proof that blocking the transaction will deny customers the merger-specific benefit.

Bazaarvoice Highlights the Courts' Narrow View of Dynamic, High-Tech Markets

In merger investigations in high-tech markets, parties often point to a broader market and to large players in adjacent markets as significant competitive constraints. Antitrust agencies have generally rejected arguments that high-tech markets should be defined more broadly because of their dynamism and alleged ease of entry and have been particularly skeptical when the merging parties point to large players such as Google, Amazon, Intel, Microsoft, and others as potential entrants. For example, in the 2012 proposed merger between Integrated Device Technologies ("IDT") and PLX Technology, two top suppliers of PCIe switches (PCIe is one of several data transfer protocols used to transmit data packets) argued that the market included numerous different technologies and that the main competitor was Intel.[9] The FTC rejected this argument, and the parties abandoned the transaction shortly after the FTC voted to challenge it in December 2012.

In *Bazaarvoice*, the parties similarly tried to paint the market as broader than just R&R, including other social commerce products such as forums, blogs, and social networks. The parties also sought to include Internet giants such as Amazon as either current players in the R&R market or "rapid entrants". Just as the FTC had done in *IDT/PLX*, the DOJ rejected these arguments. The District Court agreed, holding that social commerce products were not part of the R&R market

[7] *Id*. at 15.

[8] *Id*. at 116.

[9] *See* Press Release, FTC Issues Complaint Seeking to Block Integrated Device Technology, Inc.'s Proposed $330 Million Acquisition of PLX Technology, Inc. (Dec. 18, 2012), *available* at http://www.ftc.gov/opa/2012/12/idtplx.shtm. *See also* Julie Brill, Comm'r, Fed. Trade Comm'n, Merger Enforcement in High-Tech Markets: Address Before Skadden Arps/Compass Lexecon Symposium (Jan. 28, 2013), *available* at http://www.ftc.gov/sites/default/files/documents/public_statements/merger-enforcement-high-tech-markets/130128skaddenhightechmarkets.pdf.

because they are "fundamentally different" and "serve different purposes".[10] Similarly, the District Court did not consider the presence of Amazon to be dispositive. While the District Court noted that Amazon likely accounted for about 28% of the R&R market,[11] Amazon did not offer R&R services to third parties. Even in the face of testimony from an Amazon executive that Amazon considered entering the market "almost daily",[12] the District Court found that Amazon had not taken any concrete steps to enter the market. The District Court also observed that Google and Facebook were closer to partners of Bazaarvoice, rather than competitors in R&R. *Bazaarvoice* suggests that the agencies will continue to view high-tech markets relatively narrowly and will credit rapid entrants only where there is evidence that entry is actually occurring.

The Importance of Internal Documents

As in many past merger cases, unhelpful internal documents played a decisive role. While, as the District Court pointed out, "intent is not an element of a Section 7 violation",[13] parties' own transaction and ordinary course documents will be highly probative evidence in defining the relevant market and evaluating defensive arguments. The District Court found persuasive evidence in the parties' documents that R&R is a distinct market and Bazaarvoice and PowerReviews were duopolists in that market. Given that "the data that exist regarding this market are imperfect",[14] the District Court seemed to place greater weight on internal documents than on economic evidence in determining the relevant market. The parties' internal documents also undercut the defensive argument that the rationale for the transaction was to expand beyond R&R into new services. The District Court noted that this rationale was absent in pre-acquisition documents and there were pre-acquisition documents stating that the actual rationale was to eliminate the significant price competition from PowerReviews.

Merging parties can draw several lessons from *Bazaarvoice*: internal documents will be used by the agencies as the best evidence of parties' views of the market and bad documents will be very difficult to impeach; courts and agencies may take a narrow view of the market even where parties feel threatened by large e-Commerce companies with vast resources; lack of customer opposition alone will not prevent a successful merger challenge; and even small, non-reportable transactions continue to be targets for the authorities.

[10] *Bazaarvoice* at 46.

[11] Companies using in-house R&R solutions represented 42% of the Top 500 Internet Retailers' total revenue, and 67% of that revenue (or 28% total) was from Amazon.

[12] *Bazaarvoice* at 89.

[13] *Id.* at 21.

[14] *Id.* at 61.

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