Federal Trade Commission

Lessons Learned from United States v. Oracle Corp.

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prepared for

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Mergers, Enforcement and Standardization

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Introduction

When we talk about the future of th e merger enforcement in the technology sector, it is important to consider what we can learn from the past. I don't think anyone in the antitrust bar would disagree that the case of United States v. Oracle Corporation [1] provides a number of valuable lessons that we

The views stated here are my own and do not necessarily reflect the views of the Commission or other Commissioners. I am gratef ul to my attorney advisor, Henry Su, for his invaluable assistance in preparing these remarks.

[1] 331 F. Supp. 2d 1098 (N.D. Cal. 2004).

all can use going forward. I am here today to share some of those lessons with you.

I was one of three lead trial counsel for Oracle Corporation ("Oracle"). The other two were Dan Wall and Greg Lindstrom. They were super trial lawyers, and it was a privilege to work with them. That said, I think they too would agree that we all learned a lot from that case.

Background

The case arose out of a June 6, 2003 hostile tender offer that Oracle had made for the shares of PeopleSoft, Inc. ("PeopleSoft")—a rival in the market for the development, production, marketing and service of enterprise resource planning (ERP) software—literally on the heels of PeopleSoft's own announcement, just days before, that it had reached an agreement to acquire another market rival, J.D. Edwards. [2] Admittedly, the timing was not coincidental. Among the Department of Justice's ("DOJ") trial exhibits was a June 2, 2003 internal email exchange between Safra Catz (then an Oracle Executive Vice-President) and Oracle CEO Larry Ellison with the subject line "Psft/JDEC," in which Safra stated, "Now would be the time to launch on PSFT," and to which Larry replied, "Just what I was thinking." [3]

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[2] Specifically, PeopleSoft made its announcement on June 2, 2003, and Oracle made its tender offer on June 6, 2003. For a useful Oracle–PeopleSoft timeline, see Oracle's Bid for PeopleSoft: Timeline of Key Developments, GARTNER, INC., http://www.gartner.com/pages/story.php.id.8834.s.8.jsp (last visited Jan. 26, 2012).

[3] Government Trial Exhibit P3327, United States v. Oracle Corp., 331 F. Supp. 2d 1098 (N.D. Cal. 2004), available at http://www.justice.gov/atr/cases/f204400/204457.pdf.

PeopleSoft's reaction was immediately negative. PeopleSoft CEO Craig Conway reportedly characterized Oracle 's tender offer as "atrociously bad behavior from a company with a history of atrociously bad behavior" and compared Larry to Genghis Khan. [4] That unvarnished animosity between the two companies and their respective CEOs would give color to the ensuing

unambiguously directed at Ellison, Conw ay reportedly said that the tender offer was “like me asking if I could buy your dog so I can go out back and

Ellison and Oracle strongly suspected that Conway and PeopleSoft were "aggressively" lobbying DOJ, which had received clearance to review the transaction, to challenge the merger. [11] And indeed, the merger review process dragged on for months, into 2004. Although Conway flatly denied any lobbying, when DOJ finally decided on February 26, 2004 that it would challenge the transaction, Conway reportedly announced—triumphantly, "Now that the antitrust day of reckoning has arrived and the Justice Department has announced its decision to sue to block the transaction, it is time for Oracle to abandon its efforts to acquire the company." [12]

What Conway and PeopleSoft did not count on—or perhaps they should have anticipated—was Ellison and Oracle's willingness to take on a fight with DOJ. [13] Oracle had doggedly pursued PeopleSoft, and when DOJ staff indicated in early February 2004 that they were recommending a challenge, the company pulled out the stops with its own lobbying efforts. Not only had Oracle already hired Jim Rill, formerly head of the Antitrust Division under the senior President Bush's administration, and economist Jim Miller, a former Chairman of the Federal Trade Commission ("FTC"), to help make its case, [14] but it also hired former Senator Tim Hutchinson, a

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[11] Jaret Seiberg, DOJ to Block Oracle–PeopleSoft, THE DEAL, Feb. 27, 2004, §§ M and A.

[12] Id.

[13] Chris O'Brien, No Clear Winner As Testimony Concludes; Each Side's Closing Slated for July 20, SAN JOSE MERCURY NEWS, July 2, 2004, at 1F (describing Oracle's decision to fight DOJ as an "unusual step").

[14] Chris O'Brien, Oracle Dealt Key Setback on Hostile Bid; Justice Department Staff Opposes Offer for PeopleSoft, SAN JOSE MERCURY NEWS, Feb. 11, 2004, at 1A; In the News: Bring Out

Republican from Arkansas, to meet with staff members of the Senate Judiciary Committee, in hopes of persuading them to lean on DOJ not to accept staff's recommendation. [15] (At that time, Hew Pate was the Assistant Attorney General in charge of the Anti trust Division, and it was going to be his decision to make.)

Oracle's last-ditch political moves did not succeed, however, and DOJ filed suit in federal court in San Fran cisco. The case was assigned to Judge Vaughn Walker, a Republican appointee of the senior President Bush, and as we would later learn, a judge with a solid background in economics, having done a graduate fellowship in economics at Berkeley before going on to law school at Stanford. [16] Although Oracle had hired Jim Rill and Howrey (as well as Morrison & Foerster) to make its ca se to DOJ not to bring a challenge, when that effort was unsuccessful and the antitrust fight moved from Washington, DC to San Francisco, the company turned to us (Dan Wall, Greg Lindstrom, myself, and Latham & Watk ins), as the press reported, for our "West Coast litigation strength." [17]

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the Big Guns , July 11, 2003, MARLIN & ASSOCIATES, LLC, http://www.marlinllc.com/press-intheNews/press_id=266 (reprint of article in USAToday) (last visited Jan. 27, 2012).

[15] David A. Vise, Oracle Turns to Politics on PeopleSoft Takeover , WASH. POST, Feb. 25, 2004, at E01.

[16] Bob Egelko, The Judge Who Will Hear the Prop. 8 Case, SAN FRANCISCO CHRON., Aug. 16, 2009, at A1.

[17] Steve Hoare, Latham Elbows Out Howrey and Morrison on Oracle Battle , THE LAWYER, Mar. 8, 2004, http://www.thelawyer.com/latham-elbows- out-howrey-and-morrison-on-oracle-battle/108961.article .

Before I turn to the lessons, I should not neglect to mention that the

expect to get hired to defend the case. Whether one is meeting with an antitrust enforcement agency or arguing in front of a federal judge, the same advocacy skills are at play. In this case , when its team of advocates failed to persuade the agency, Oracle felt that it needed a new team of advocates to tell its story to the judge.

Lesson 2: Do not challenge a merger in the A side's home court, however tempting that may be.

A lesson for DOJ—and the FTC as well—is not to challenge a merger in the A side's home turf. If it can't be Washington, DC, pick a neutral forum instead. Of course, perhaps DOJ can be forgiven for making this mistake in the Oracle case. PeopleSoft, which was a hostile B side, also called the San Francisco Bay Area home (Pleasanton, to be precise), and that is probably why the case was brought there instead of in Washington.

Lesson 3: Do not define the relevant product market based on the preferences of certain customers.

When DOJ announced that it was challenging the merger, it had already painted the transaction as a case of three firms (SAP, Oracle, and PeopleSoft) m6hon.

that we have a product that only three firms are in a position to provide." [21] Oracle responded to this assertion by saying, "[DOJ's] claim that there are only three vendors that meet the needs of large enterprises does not fit with the reality of the highly competitive, dynamic and rapidly changing market." [22] This debate over what vendors competed in the relevant product market would become a focal point of the bench trial, and DOJ's excessive reliance on customer testimony would come back to haunt it.

Specifically, in his opinion, Judge Walker concluded, "In the main, and contrary to the characterization of plaintiffs' counsel before trial, the court found the testimony of the customer witnesses largely unhelpful to plaintiffs' effort to define a narrow market of high function FMS [financial management systems] and HRM [human relations management]." [23] While he found DOJ's customer witnesses to be knowledgeable and sincere, their testimony could not carry the day for DOJ's case because they were really testifying about their own preferences, and not "about what they would or could do or not do to avoid a price increase from a post-merger Oracle," which was the gating issue for product market definition. [24] And insofar as the customer witnesses

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[21] Alex Pham, U.S. Regulators Oppose Oracle's PeopleSoft Bid, L.A. TIMES, Feb. 27, 2004, at 2.

[22] Id.

[23] United States v. Oracle Corp., 331 F. Supp. 2d 1098, 1130, 1131 (N.D. Cal. 2004).

[24] Id. at 1131 ("Customer preferences towards one product over another do not negate interchangeability…. The preferences of these customer witnesses for the functional features of PeopleSoft or Oracle products was evident. But the issue is not what solutions the customers would like or prefer for their data processing needs; the issue is what they could do in the event of an anticompetitive price increase by a post-merger Oracle.").

had attempted to address the question of their likely response to a SSNIP by a post-merger Oracle, Judge Walker found such testimony to be speculative and unsupported by any hard evidence or analysis. [25]

Ken Heyer, a DOJ economist, has termed this seeming inability of

witnesses must be numerous enough to be "representative," [29] and yet not too numerous as to bore the court to tears. [30] It is very hard, if not impossible, to thread that needle. Additionally, Judge Walker would later quip in an article he had written, "A special brand of ju dicial skepticism is reserved for a parade of witnesses beating the same drum." [31]

Lesson 4: Do not define the relevant geographic market in a fashion that is at odds wi th what your economist has written.

In Oracle, DOJ called Professor Kenneth Elzinga as one of its economist experts. [32] Anyone in the antitrust bar would have applauded this

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[29] United States v. Engelhard Corp., 126 F.3d 1302, 1306 (11th Cir. 1997) ("No matter how many customers in each end-use industry the Government may have interviewed, those results cannot be predictive of the entire market if those customers are not representative of the market."); Feesers, Inc. v. Michael Food s, Inc., 632 F. Supp. 2d 414, 445 (M.D. Pa. 2009) (holding that "testimony presented by Defendants from a few customers who did not find

choice, as Elzinga is accomplished and highly respected in antitrust circles. In this case, however, DOJ's choice proved to be a mistake given the case that it wanted to present.

As you probably know, Elzinga co-developed the Elzinga–Hogarty test for use in defining a geographic market.[33] Applying that test, the relevant geographic market in this case was undisputedly a worldwide market, as Judge Walker noted.[34] But DOJ was arguing for a United States market, and Elzinga was therefore put in the awkward position of having to tell Judge Walker that his "oft-used" test was not applicable here.[35] That position was at best confusing to the judge. At worst, it destroyed Elzinga's credibility.[36]

Lesson 5: Do not believe it when your economist says that pricing is too opaque to support a coordinated effects theory.

There are lots of other ways that rivals can coordinate their behavior despite opaque pricing—for example, through market or customer

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[33] The Elzinga–Hogarty test has been described by the courts as "measur[ing] the accuracy of a market delineation by determining the amount of either imports into or exports from a tentative market. The test is based on the assumption that if an area has significant exports or imports, then that area is not a relevant geographic market. Under the [test], exports or imports greater than 10% suggest that the market examined is not a relevant market." United States v. Country Lake Foods, Inc., 754 F. Supp. 669, 672 n.2 (D. Minn. 1990).

[34] United States v. Oracle Corp., 331 F. Supp. 2d 1098, 1164 (N.D. Cal. 2004) ("Furthermore, the results of employing the E-H test are undisputed. See Tr at 2155:9–10 (Elzinga) (admitting that the E-H test would dictate the court to view the market as a global market).").

[35] Id. at 1161 ("In reaching this [United States] market definition, Elzinga ironically enough did not rely upon the oft-used Elzinga-Hogarty (E-H) test, which he admitted has been used in 'dozens and dozens of merger cases' and which he himself co-developed. Tr at 2154:22–23 (Elzinga).").

[36] Id. at 1164 ("Elzinga's basis for rejecting the E-H test is unpersuasive.") & 1165 ("Elzinga, creator of the test, admitted that applying the E-H test would mandate a global market. The court therefore finds that the geographic market in this case is global.").

allocation.[37] A 2009 district court decision in a merger case brought by the FTC, CCC–Mitchell, illustrates this point.[38] Yet, in Oracle DOJ did not make a coordinated effects claim until the eleventh hour—after the trial record had closed.[39] By then it was too late.[40]

Lesson 6: Designate a respected spokesperson for the company to deal with the press.

In Oracle Dan Wall was that person. Every night after court he would stroll into the mob of reporters and explain to them what they had just heard in words of one syllable—for example, I first heard the expression "whack a mole" from Dan. (For anyone who doesn't yet know the meaning of this expression, I have included a citation to William Safire's On Language column in the footnotes to my remarks.)[41] Oracle went from a forlorn

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[37] See U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, HORIZONTAL MERGER GUIDELINES § 7.2 (2010) ("Even if terms of dealing are not transparent, transparency regarding the identities of the firms serving particular customers can give rise to coordination, e.g., through customer or territorial allocation."), available at http://www.justice.gov/atr/public/guidelines/hmg-2010.pdf.

[38] FTC v. CCC Holdings Inc., 605 F. Supp. 2d 26, 64–66 (D.D.C. 2005) (noting that pricing is not the only type of "key information" that can be used to facilitate coordination, and that a mature market with "little room for growth" may supply conditions that "can lead to even greater stabilization of market share and greater segmentation of the market, thus increasing the incentives and lowering the impediments to tacit coordination.").

[39] Oracle, 331 F. Supp. 2d at 1165, 1166 ("Plaintiffs presented no evidence at trial on coordinated effects. … But in plaintiffs' post-trial brief they unexpectedly included an entire section arguing that a post-merger Oracle and SAP could tacitly collude in allocating customers or markets."). See also Dawn Kawamoto, Judge's Order May Be Good for Oracle, CNET NEWS (July 12, 2004, 3:51 PM), http://news.cnet.com/Judges-order-may-be-good-for-Oracle/2100-1011_3-5266345.html?tag=txt (referring to Judge Walker's request to the parties for post-trial submissions clarifying the nature of, and the support for, the unilateral effects theory of harm advocated by the government).

[40] Id. at 1166 ("With no evidence in the record regarding such a speculative coordinated effects argument, the court finds this new theory to be without merit.").

[41] William Safire, On Language: Whack-a-Mole, N.Y. TIMES, Oct. 29, 2006, http://www.nytimes.com/2006/10/29/magazine/29wwln_safire.html ("The origin is in the old

underdog in the press's view to the favorite … and we won the defense verdict of the year. [42]

When litigating merger cases, one has to remember that cases are not decided in a vacuum, especially if the case is high-profile and the trial is lengthy. Judges read the papers, watch television and surf the net the way the rest of us do. It is important that they not get the impression that the case they are deciding is either a slam dunk or a lost cause. The merging parties and their public relations people spend a lot of money making sure that a case of this kind is fairly reported.

Cognizant of the press's great interest in the case, both Dan and Oracle pushed for a more open trial, even though it would mean that the company would have to disclose some of its own closely held information. [43] Not only did this strategy allow the case to be tried in the court of public opinion as well as the court of law, but it also appealed to a trial judge's sensibilities about the courts needing to be open public forums where the public can see justice in

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carnival or arcade game that has a mechanical mole suddenly appear for a player to knock down, which causes another object to appear.").

[42] June D. Bell, Top Defense Win of 2004: Deft Defense Picks Apart the DOJ, NAT'L L.J., Mar. 28, 2005.

[43] Michael Liedtke, Oracle Antitrust Judge May Unseal Evidence, CRN (June 11, 2004, 9:00 AM), http://www.crn.com/news/applications-os/21700311/oracle-antitrust-judge-may-unseal-evidence.htm;jsessionid=AmLSth7WhB-usE+P+pOPrw**.ecappj03 (quoting Dan Wall as saying, "Oracle very clearly wants this to be an open trial.").

action.[44] Certainly that was the case with Judge Walker, as we all know from Oracle and the more recent Proposition 8 trial.[45]

Lesson 7: Designate someone to deal with your most important, but difficult, witness.

In Oracle that witness was Larry Ellison, and because I had the most grey hair, I was designated to deal with him in the board room. The first day he pontificated at length about how we were going to win the case. I spoke up and said there was only one person in the courtroom whose opinion mattered (referring to the judge), and it was not Larry. After the board exhaled, he said quietly that he'd remember that, and

outrageous remarks, in court he was cool and unflappable. Pressed by Scott [the government's lead trial lawyer] to agree that innovation would suffer as a result of PeopleSoft's disappearance, Ellison suggested that his cross-examiner was on another planet." [46]

Lesson 8: On the other hand, don't designate that same person to deal with the second most difficult, but important, witness.

In Oracle that witness was Safra Catz, who was Oracle's co-president and the author of our efficiencies study. My wife, Kitzi, thought Safra was the smartest and best witness she had ever seen. But efficiencies was one of only two defenses that we lost at trial, [47] and that may have been my fault. Or it may be because the judge wanted to throw DOJ a bone. [48]

Lesson 9: Have your most skilled trial lawyer interrogate witnesses that are not hostile witnesses.

The most skilled trial lawyer in the Oracle case was undoubtedly Greg Lindstrom. Why? Because witnesses that are not hostile cannot be led or otherwise cross-examined if the trial judge is worth his salt. [49] It takes intuition and guts to interrogate them "cold." As all good trial lawyers know,

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[46] Karen Southwick, Perspective: Ellison's Defining Moment, CNET NEWS (July 2, 2004, 12:30 PM), http://news.cnet.com/Ellisons-defining-moment/2010-1001_3-5256253.html?tag=txt.

[47] United States v. Oracle Corp., 331 F. Supp. 2d 1098, 1175 (N.D. Cal. 2004) ("The court finds Oracle's evidence on the claimed cost-savings efficiency to be flawed and unverifiable.").

[48] Id. at 1108–09 (finding for Oracle on all issues except for its efficiency defense and its argument that the relevant product market included products in the integration layer of the "software stack").

[49] FED. R. EVID. 611(b) & (c) (making clear that leading questions should not be allowed on

to be effective, direct examination sh ould not sound rehearsed or scripted. Time and again, Greg demonstrated th at he was up to that challenge.

Lesson 10: On the othe

Lesson 11: Be sure that the only sources of th

Lesson 12: Rely on the Merger Guidelines as much as possible.

In the Oracle case, DOJ's principal theory of antitrust harm was a unilateral effects theory described in the then Section 2.2 of the 1992 Horizontal Merger Guidelines. [56] Those Guidelines seemed to state that DOJ needed to prove that the parties were each other's best substitutes and they combined had at least 35% of the market. [57] We stressed that requirement in the Guidelines over and over again, and Judge Walker duly took note of it. His rulings dealt with the Guidelines requirement in two respects.

First, Judge Walker concluded that "[a] presumption of anticompetitive effects from a combined share of 35% in a differentiated products market is unwarranted. Indeed, the opposite is likely true." [58] He held instead that "[t]o prevail on a differentiated products unilateral effects claim, a plaintiff must prove a relevant market in which the merging parties would have essentially a monopoly or dominant position." [59] This significantly raised the bar on DOJ's burden to establish combined market shares for

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[56] U.S. DEP'

Oracle and PeopleSoft high enough to be presumptively unlawful under the Guidelines. [60]

Second, we gave Judge Walker our own estimates of combined market shares for Oracle and PeopleSoft for the worldwide FMS and HRM markets, and they were both below the 35% threshold under the Guidelines. [61] Although Judge Walker did not find our estimates to be definitive and reliable, it didn't matter because as he noted, "it is plaintiffs, not defendant, who carry the burden of proving market shares and concentration in order to invoke the presumptions of the case law or to sustain a showing in accordance with the Guidelines. The court cannot furnish its own statistics." [62] He therefore found that DOJ had "not proved that the post-merger level of concentration (HHI) in the product and geographic markets, properly defined, falls outside the safe harbor of the Horizontal Merger Guidelines[.]" [63]

When trying a merger case, always remember who has the burden of proof. It is a point that I frequently remind the FTC staff whenever we are considering an enforcement action.

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[60] See id. at 1148 (DOJ's economist expert calculating combined Oracle–PeopleSoft market shares of 48% and 68% of the United States high function FMS and HRM markets, respectively).

[61] See id. at 1164 (Oracle offering combined Oracle–PeopleSoft market shares of 28.8% and 14.3% of the global high function FMS and HRM markets, respectively).

[62] Id. at 1165.

[63] Id. at 1108.

Lesson 13: On the other hand, don't rely on what the judge says during argument or even when interrogating witnesses.

All three of us agreed that Judge Walker would try to keep the ball in the air throughout closing argument.[64] As a result, the press and even Tom Barnett, then the Deputy Assistant Attorney General for Antitrust, thought DOJ had won the case.[65] However, in questioning the witnesses, Judge Walker noted (and emphasized) that the parties sold other products besides the HRM and FMS software in question as "bundles" to customers. That seemed to us to be a brand new defense theory, and it was consistent with teaching in the case law that a relevant product market is not necessarily confined to similar, interchangeable products, but in some instances, may involve clusters of dissimilar products or services.[66] We were wrong.

Lesson 14: Be lucky enough to have a savvy judge.

We drew Judge Walker, who loved the case and was a skilled economist to boot.[67] Not only that, but he was smart enough to base his decision on the facts, as evidenced by his 164-page opinion thoroughly analyzing the record. That made it very hard for DOJ to appeal. As Tom Barnett reportedly acknowledged, "The court of appeals would give [Judge

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[64] Alorie Gilbert, Judge Grills Oracle, DOJ, at Trial's Close, CNET NEWS (July 20, 2004, 4:34 PM), http://news.cnet.com/Judge-grills-Oracle%2C-DOJ-at-trials-close/2100-1012_3-5276907.html?tag=txt.

[65] O'Brien, supra note 13 (quoting Tom Barnett, Deputy Assistant Attorney General for Antitrust, as saying, "I don't believe they made their case, period. I think they raised a lot of distractions.").

[66] See, e.g.,Westman Comm'n Co. v. Hobart Int'l, Inc., 796 F.2d 1216, 1221–22 (10th Cir. 1986); JBL Enters., Inc. v. Jhirmack Enters., Inc., 698 F.2d 1011, 1016–17 (9th Cir. 1983).

[67] See supra note 16 and accompanying text.

Walker's factual] findings a lot of defe rence. If you accept his factual findings, it's hard to show the me rger is anticompetitive." [68]

approach in the Oracle case, he concluded that DOJ's evidence, as presented through its customer witnesses and it s economist expert, did not match up with its story of harm: "There was a disconnect between the economic analysis the government sought to relate and the storytellers it brought to court." [72]

Lesson 15: The EC can always stop the clock on an investigation.

The last lesson I will offer you is the observation that the EC can always stop the clock on a merger investigation it is conducting. In Oracle, the EC stopped the clock (for a second

office.[75] Moreover, the EC's legal services team following the investigation had reportedly been opposed to a prohibition decision for several months, and Commissioner Monti was known to accord them a lot of deference.[76] It was therefore only a matter of time before the EC cleared the merger as well, which it did on October 26, 2004.[77] No one was surprised by the news.

Aftermath

Notwithstanding its triumphs in the legal battles, Oracle did not successfully complete its hostile takeover of PeopleSoft until it offered to pay $26.50 a share in December 2004.[78] By January 7, 2005, more than 97% of the shares of PeopleSoft stock had been tendered under the offered price, and Oracle was then able to expedite its takeover under Delaware law.[79]

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[75] Cordes, Clear, supra note 18.

[76] Meller, supra note 18.

[77] Benjamin Pimentel, EU Clears Way for PeopleSoft Takeover, SAN FRANCISCO CHRON., Oct. 27, 2004, at C-1, http://www.sfgate.com/cgi-bin/article.cgi?f=/c/a/2004/10/27/BUG949GR2I1.DTL.

[78] Paul R. La Monica, Finally, Oracle to Buy PeopleSoft, CNN/MONEY (Dec. 13, 2004, 12:53 PM), http://money.cnn.com/2004/12/13/technology/oracle_peoplesoft/.

[79] Charles Babcock, Oracle Completing PeopleSoft Takeover Today, INFORMATION WEEK (Jan. 7, 2004, 12:48 PM), http://www.informationweek.com/news/57300414.