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I. Introduction

On Friday, January 10, 2020, the Department of Justice (DOF) and the Federal Trade Commission (FTC) jointly released new Draft Vertical Merger Guidelines (the "Guidelines" or "Draft Guidelines"),[3] and sought public comment.[4] On February 3, 2020, the FTC and DOJ extended the comment period until February 26, 2020.[5] The Draft Guidelines are the first time DOJ and the FTC have sought to update their approach to vertical mergers since 1984, and come on the heels of the DOJ's failure to stop the merger between Time Warner (a video programmer) and AT&T (a pay-TV distributor) in the first merger review to be decided by the courts in four decades.[6]

TechFreedom is a non-partisan think tank dedicated to promoting the progress of technology that improves the human condition. To this end, we seek to advance public policy that makes experimentation, entrepreneurship, and investment possible, and thus unleashes the ultimate resource: human ingenuity. Wherever possible, we seek to empower users to make their own choices online and elsewhere.

We study how the law governs iniFGeris i

Revolution—characterized by creative destruction, constant paradigm shifts, and the near-constant introduction of disruptive technologies.

Vertical integration is an essential aspect of the Digital Revolution. In the constant tumult to manage new paradigms of using technology and doing business, firms are perpetually looking both to acquire technology, talent, business relationships and other inputs of the competitive process through acquisition—and other firms, especially smaller firms, are always looking to be acquired.[9] Among economists, there is a clear consensus that technology-related vertical mergers are generally efficiency-enhancing, for two reasons. First, as Prof. Daniel Sokol notes, "[v]ertical acquisitions involving technology start-ups are "largely comple-

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between markets are especially difficult to define, where products change faster than regulators and courts can change the mental models they use to understand the real world, and where business model innovation is no less vital than technological innovation.

serve political interests. We believe there is good reason to worry about both possibilities, as we discuss more fully below.

A. The Life Cycle of Technology Behemoths Is Short

For the last quarter century, the digital world has been uniquely dynamic, with tech giants appearing dominant for regularly brief periods, but eventually struggling to avoid seeing their dominance disrupted just as they themselves disrupted the companies they once displaced. The title of Clayton Christensen's 1997 classic book sums up the problem aptly: Innovator's Dilemma: When New Technologies Cause Great Firms to Fail.[13]

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Nokia's one billion customers and decried, "Can Anyone Catch the Cell Phone King?"[18] Well, the market did, and Nokia was dead within 10 years, when Microsoft wrote off its 2014 $7.2 billion acquisition of Nokia—another vertical merger gone bad.[19] Nokia failed to see the coming wave of smartphones, and never realized that what would drive the market was not better hardware form factors, but software that could handle larger data uses and provide easier access to the growing assets of the Internet.[20]

In 2010 Apple's iTunes was declared by some as a "monopoly," with calls for its dismantling.[21] But that was before the emergence of music streaming services such as Spotify and Pandora. Today, Apple's share of the market today is around 20 percent—very far from a monopolist position.[22]

Then there was MySpace. Those under 40 might ask "Who Space?" MySpace was (technically it still is an "is," as it had 50 million registered users in 2015 and 15 million monthly subscribers in 2016)[23] a social media sharing platform that experts deemed a "natural monopoly" in 2007.[24] Critics warned of the dangers of allowing media mogul Rupert Murdoch to acquire such a platform in 2005 for $580 million. "[A]s the MySpace generation goes into employment, [the platform] could eventually extend Murdoch's influence in ways that would make his grip on satellite television seem parochial."[25] According to these same critics, only Bebo.com (who?) or Cyworld.com (who?) had a chance to catch this runaway train. And that would be next to impossible, according to experts at the time:

> It is common knowledge that a fax machine is worthless until others have one too. That is what is happening in social networking except that, unlike a fax machine, it can't be instantly swapped for another. It is easy to change search

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[18] James Waterworth, Lessons From Nokia's Demise—The Cost of a Fragmented Developer ExperienceThIloor,hc asThwwoul

engines, even if it is Google. But if you change social networks you not only have to move all your videos, audios, messages, photos elsewhere but you also lose your network of friends unless they migrate with you. MySpace won't make that easy. Its massive user base will help maintain its dominance, according to co-founder Chris DeWolfe. "In social networking, there is a huge advantage to have scale. You can find almost anyone on MySpace and the more time that has been invested in the site, the more locked in people are.[26]"

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A report recently leased by the President's Council of Economic Advisors reaches the same conclusion:

> In markets with network effects or other types of economies of scale, firms may compete for the entire market, rather than for shares in the market. The resulting monopolies may not be permanent. Bourne (2019) gives many examples of firms that achieved dominance through network effects or production economies of scale, only to eventually lose out to competition from innovative rivals. His examples range from the Great Atlantic & Pacific Tea Company in the 1920s to MySpace and Nokia in the early part of this century.[30]

Yet, if we believed the rhetoric of the current "Techlash" and the so-called "hipster antitrust" movement, one would think that time has stopped, the Internet has fully matured,[31] and the process of technological disruption has ceased. WYSIWYG—"what you see is what you get," and we must analyze markets, and assess consumer welfare, based on the assumption that markets will never change going forward. We must ignore the fundamentally disruptive technologies of artificial intelligent (AI), virtual reality (VR), augmented reality (AR), and the Internet of Things (IOT) just over the horizon. We must ignore the revolution in mobile applications and services that the giant "pipes" of 5G communications will make possible. Approaching antitrust law from this perspective, and writing the Vertical Merger Guidelines accordingly, risks jeopardizing the dynamism of the entire U.S. economy, which is increasingly driven by its technology sector.[32]

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[30] Economic Report of the President Together with the Annual Report of the Council of Economic Advisers at 218 (Feb. 2020) (hereinafter "2020 Economic Report of the President") (citing Ryan Bourne, Is This Time Different? Schumpeter, the Tech Giants, and Monopoly Fatalism, CATO Institute (June 17. 2019), https://www.cato.org/publications/policy-analysis/time-different-schumpeter-tech-giants-monopoly-fatalism), https://www.whitehouse.gov/wp-content/uploads/2020/02/2020-Economic-Report-of-the-President-WHCEA.pdf.

[31] This approach is manifest in Commissioner Chopra's statement accompanying the release of the draft Vertical Merger Guidelines: "First, enforcers need to be more thorough about assessing each firm's existing dominance. A rigorous investigation must rely on a full inventory of the means by which each company has achieved, maintains, or ex8n (e)-1 (n)9.1(o)-0.5eo

B. The Draft Guidelines Will Greatly Increase the Discretion of the Government, Particularly in High-Tech Cases

Commissioner Chopra argues that "there should not be a presumption that all vertical mergers are benign."[33] While the draft guidelines do not appear to go quite this far, they would give too much discretion to regulators in policing vertical transactions. As Herb Hovenkamp, author of the leading treatise on antitrust law,[34] notes, "[w]hile the new draft Guidelines leave the overall burden of proof with the challenger, they have clearly weakened the presumption that vertical mergers are invariably benign, particularly in highly concentrated markets or where the products in question are differentiated."[35] The limited safe harbor afforded by the draft Guidelines comes in the following form:

> The Agencies are unlikely to challenge a vertical merger where the parties to the merger have a share in the relevant market of less than 20 percent, and the related product is used in less than 20 percent of the relevant market.[36]

Like Jan Rybnicek, former Attorney Adviser to FTC Commissioner Wright, we fear that this supposed safeguard will, in practice, mean "that agency staff will soon interpret (despite language stating otherwise) the 20% market share as the minimum necessary condition to open an in-depth investigation and to pursue an enforcement action."[37] As Jonathan Nuechterlein, former General Counsel of the FTC, complains, "This anodyne assurance, with its arbitrarily low 20 percent thresholds phrased in the conjunctive, seems calculated more to preserve the agencies' discretion than to provide genuine direction to industry." He continues:

> Quoting then-Judge Breyer, the Supreme Court once noted that "antitrust rules 'must be clear enough for lawyers to explain them to clients.'" That observation rings doubly true when applied to a document by enforcement officials purporting to "guide" business decisions 6 Tc (i)1.9 eere61.9 he awas.8 (cs.8 (cTd 7 Tw --0.6 (an0.7 (lc)0.5

candle, particularly given the empirically validated presumption that most vertical mergers are pro-consumer.[38]

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- The new guidelines would dramatically reduce the weight that will be given to claimed efficiencies in vertical transactions. The 1984 guidelines recognize that: "

they conclude their transactions quickly. Firms considering vertical integration may abandon efficiency-enhancing transactions simply because, contrary to Justice Breyer's urging, "antitrust rules" are not "clear enough for lawyers to explain them to clients."[46]

This would represent a significant a significant shift in the v

$100 million in market capitalization did not have any research coverage. The result is alarmin

However mighty they may seem, no company struggling to avoid the “Innovator’s Dilemma”[58] can today afford anything like the ordeal Microsoft endured. This desperation for speedy approval, even from positions of apparent strength, makes such firms vulnerable to extortion through the merger review process, both by their rivals, who demand either that the deal be blocked or be conditioned in ways that advantage them, or by politicians with an ax to grind against the firm. The need to get the deal done, the time, expense and negative publicity associated with litigation, and the fact that the FTC may choose to pursue a case through its internal administration process, means that merging parties must slog through trial before an administrative law judge, and then another layer of review by the full Commission before having access to a federal court—these factors all combine to give the government enormous power to punish companies by challenging their mergers, or to demand conditions for merger approval. As former Commissioner Josh Wright notes:

> feature content in the "Trending" section at the top corner of its homepage. Facebook responded to concerns about the left-wing slant of the employees who screened content suggested as "Trending" by algorithms on a rolling basis by simply ending human involvement in the process. This significant change in how Facebook operated its site was troubling enough as a roadmap for how to circumvent the First Amendment; it also had disastrous consequences, making it far easier for Russian and other foreign actors to manipulate Facebook's algorithms to get their misinformation content featured prominently on Facebook — thus favoring those candidates and causes [which] foreign interference was intended to aid.[63]

The very murkiness of how social media work makes political meddling easier and less detectable.

A. Recent Politicization of the DOJ and the Antitrust Division.

Since Watergate, the Antitrust Division has rebuilt its reputation for integrity. The necessary prerequisite for this rehabilitation wa[illegible]

Everyone who has worked at the DOJ and the FTC should take pride in what antitrust law has become—not without its flaws, to be sure, but at least the product of a process that inspires confidence. Or such was the situation before the current administration.

In recent years, the Department of Justice has been politicized in ways unprecedented since the Nixon administration. President Trump

These are just a few examples of a much larger, troubling pattern that has caused many to lose confidence in the DOJ's current leadership. Unfortunately, there is also good reason to think this pattern extends to the Antitrust Division: after years of relentless public complaints from Trump about CNN—Trump's bête noire, just as The Washington Post was Nixon's—the DOJ sued to block AT&T's acquisition of Time Warner, the first suit to block a vertical merger case since 1977.[67] Jonathan E. Nuechterlein, counsel for AT&T, provides a concise summary of the weakness of DOJ's case—and rightly complains that the DOJ seems to have learned the wrong lesson from losing a case that clearly should never have been brought:

> DOJ ultimately conceded that Time Warner was unlikely to withhold programming from ("foreclose") AT&T's pay-TV rivals. Instead, using a complex economic model, DOJ tried to show that the merger would increase Time Warner's bargaining power and induce AT&T's pay-TV rivals to pay somewhat higher rates for Time Warner programming, some portion of which the rivals would theoretically pass through to their own retail customers. At the same time, DOJ conceded that post-merger efficiencies would cause AT&T to lower its retail rates compared to the but-for world without the merger. DOJ nonetheless asserted that the aggregate effect of the pay-TV rivals' price increases would exceed the aggregate effect of AT&T's own price decrease. Without deciding whether such an effect would be sufficient to block the merger—a disputed legal issue—the courts ruled for the merging parties because DOJ could not substantiate its factual prediction that the merger would lead to programming price increases in the first place.
>
> It is unclear why DOJ picked this, of all cases, as its vehicle for litigating its first vertical merger case in decades. In an archetypal raising-rivals'-costs case, familiar from exclusive dealing law, the defendant forecloses its rivals by depriving them of a critical input or distribution channel and so marginalizes them in the process that it can profitably raise its own retail prices (see, e.g., McWane; Microsoft). AT&T/Time Warner could hardly have been further afield from that archetypal case. Again, DOJ conceded both that the merged firm would not foreclose rivals at all and that the merger would induce the firm to lower its retail prices below what it would charge if the merger were blocked. The draft Guidelines appear to double down on this odd strategy and portend more cases predicated on the same attenuated concerns about mere "chang[es in] the terms

[67] See supra note 6.

> of … rivals' access" to inputs, unaccompanied by any alleged structural changes in the competitive landscape.[68]

"Unclear," indeed! But there is good reason to suspect that, whatever DOJ staff handling the case might have thought

> Trump often “vented” in “frustration” about wanting to block the A.T. & T.-Time Warner merger. “The President does not understand the nuances of antitrust law or policy,” the former official says. “But he wanted to bring down the hammer.” (Last month, a federal court ruled against the Justice Department.)[69]

As with Nixon, it may take years for reporters and historians to develop a full accounting of
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But even this apparently vital difference between the FCC's review process and antitrust merger review process may not be as large as it appears on paper. If parties to a transaction feel enough pressure to conclude their deal, especially if the law is sufficiently vague, and if the government can drag out the process of merger review and litigation long enough, the same dynamic may result under antitrust review, even though the burden of proof remains with the government. The chief difference would remain: the FCC would essentially never have to sue to hold a company hostage, because the deal could not be consummated until the Commission granted approval. By contrast, the DOJ or FTC could only drag out the review process so long and would eventually have to sue to block the deal. But if the antitrust agencies can drag out the process long enough, both the filing of the suit and the litigation process, the result may be precisely the same: using the threat of litigation to coerce companies and extract concessions from them. There is good reason to fear that the government's decision to sue may, itself,

radio station. The Lorain Journal Co. rule thus does not authorize restrictions on a speaker's editorial judgment about what content is more valuable to its readers.[78]

Such is the theory of the First Amendment. In practice, government has used antitrust law to retaliate against media for the content of their coverage. In the far simpler media landscape of 1972, The Washington Post was vulnerable to political retaliation by the White House even though the First Amendment has always protected newspapers from government licensure because The Post also owned broadcast stations, which were licensed by the government. When it came time for those licenses to be renewed, Nixon attempted to wield power through his pliant FCC Chairman.

Today, such cross-media integration is more common, more important and more complicated. A few examples illustrate just how difficult it is to distinguish "new" from "old" media or to pigeon-hold companies into narrow product markets:

- Most obviously, The Post is now owned by Jeff Bezos, who also owns Amazon, a company that began by selling books online then expanded into selling pretty much any consumer good, bought one of America's leading grocery stores along the way, built a network of servers relied upon by many businesses in America, launched a streaming service that's free to anyone who pays for a subscription mainly marketed as a way to get free two-day shipping, and started a studio to produce film and television shows—just to name a few highlights.
- The AT&T case involved America's second largest wireless carrier, which also owns America's largest satellite television distributor, and which serves millions of Americans with broadband, buying one of the largest conglomerates of traditional video programming, including CNN, one of Americas' most influential media channels.
- Comcast, Americas' largest broadband network, also owns NBC Universal, including traditional NBC broadcast stations and the content produced by stati

These complicated services were largely formed through the kind of vertical transactions that would be subject to review under the draft guidelines—and each will, doubtless, continue to evolve through vertical transactions. The list barely begins to mention the many smaller companies that each of these larger companies acquired along the way. This is simply how large companies attempt to avoid the "Innovators Dilemma," to stay relevant as techno-
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[8] In terms of non-horizontal transactions, more mergers are motivated by a firm's desire to expand its data estate. According to the OECD, 'big data related' mergers and acquisitions rose from 55 in 2008 to 134 in 2012. This desire for analytic capabilities and new data, particularly when used to feed and train artificial intelligence, can impact the competitive landscape in ways that limit new entry. This is not limited to internet platforms or consumer-facing businesses[81]

pa4.0.5 .oB-.6 (lepa)4. Chopra goes on to claim that: ess13 [(:)T*.9 pd d00-1-1a -0.6 ())0.6 (n h(t3.2.9a-)3 (n d)5.9 (0)0-0.0bTJ2-8

The merging parties' non-replicable assets, including control of essential intellectual property, infrastructure, and even data, may provide dominance, espec t[i0.6 (r)3.9 (I (p)-3.(p)-

antitrust law remains little better developed than it was in 2007: while academics have certainly written about the topic, there does not exist the kind of case law that would justify including something about this topic in the Vertical Merger Guidelines.

B. Increased Incentive to use "Government-Granted Benefits"

Cmr. Chopra proposes to add an additional level of analysis to merger review:

> [E]nforcers need to be realistic about predicting the likely ways that the merger will incentivize or allow firms to distort competition by extending or enhancing their existing dominance. Understanding the deal rationale is key here, as it is likely to be linked to new ways to leverage market power. This requires a careful inquiry into all the incentives and opportunities that can lead to harm... Will the merged firm have an incentive to gain an upper hand using government-granted benefits such as intellectual property rights or legal immunity?[84]

We share his concern about crony capitalism, i.e., the potential for powerful firms to manipulate the government to their own advantage. But we do not see how the theoretical possibility that a merged company might gain a greater ability to "gain an upper hand using government-granted benefits" would mean in practice. It is particularly unclear what Chopra is referring to with his mention of "legal immunity."

C. "Regulatory Evasion"

Commissioner Slaughter is "particularly concerned that the Guidelines … fail to mention regulatory evasion as a theory of harm."[85] Her use of the term "regulatory evasion" may confuse many readers. As her footnote makes clear, the kind of regulation this refers to is rate regulation, not regulation generally:

> In 2008, the FTC brought a vertical merger action based on this theory—that a firm can evade rate regulations by acquiring an upstream input and raising the cost of that input, which can lead to a regulator to authorize a higher downstream regulated rate based on that higher input cost.[86]

There is no recognized theory by which a merged firm's increased ability to "evade regulation" generally should constitute grounds for blocking or conditioning that merger—and for

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[84] Chopra Statement, *supra* note

good reason. Such a theory would introduce far too much uncertainty into the antitrust laws and give far too much discretion to regulators.

V. Conclusion & Specific Recommendations

In 2018, Josh Wright's Global Antitrust I

FCChas, more

We recognize that completely transferring responsibility for media-related companies to the FTC will seem radical to some and raises thorny problems regarding personnel. We believe it is essential to protect free speech from political meddling as the Digital Revolution continues to transform the media landscape, making media companies more vulnerable than ever to pressure from the government through the selective application of antitrust law. As second-best reform, it would be beneficial to clarify the clearance process by which the two agencies resolve disputes over which agency will handle a particular case. Greater predictability as to that question would at least help to reduce the potential for political gamesmanship through the selection of the DOJ as the agency more willing to do the bidding of the Administration.

In closing, we emphasize that while the last three years of the Trump Administration have raised significant concerns about the potential for the antitrust laws to be abused, these concerns are not unique to this administration, nor will they be resolved simply by a change in partisan control of the White House. Our concerns are systemic and could arise under a president of either party. There is simply no way to tell what the future will bring, but we do expect that the susceptibility of media companies to political pressure through, among other tools, the antitrust law—and, in particular, the potential for extortion through the merger review process—will only grow. Just as the 1984 Non-Horiret(a)5 (nd)2 02 Tc -0.042 Tw 0.10.015er p