MERGER ENFORCEMENT IN HIGH-TECH MARKETS
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SKADDEN ARPS/COMPASS LEXECON SYMPOSIUM

1. Introduction

Good afternoon everyone. Thanks to Sharis Pozen, Skadden Arps, and Compass Lexecon for inviting me here today. They have asked me to speak to you about merger enforcement policy in the high-tech sector. So you can blame them, and not me, for the fact that I'm not going to address the FTC's recent Google investigation.

But just so I'm not accused of ignoring the elephant in the room, I'll note that the FTC's recent investigation regarding Google's practices with respect to search and standard essential patents is the agency's fourth Google case since I became a Commissioner two and a half years ago. We have conducted two privacy investigations, the first culminating in a consent decree[1] and the second in the largest fine the agency ever obtained in a privacy matter.[2] And we conducted an extensive investigation of the *Google/AdMob* merger in 2010,[3] which landed at the agency's doorstep right around the time I joined the Commission, triggering a Google learning curve at the agency that continues to this day.

In light of the recent – some might say relentless – focus on Google, I hope you will understand why I am pleased that Sharis has given me the opportunity to talk to you today about a high-tech competition case to which that company was not a party. What I would like to do is speak to you today about the attempted merger between Integrated Device Technologies and PLX Technology, which was abandoned last month shortly after the Commission voted to challenge it.[4] Although Google occupied much of the FTC's time during the past several months, in many ways IDT/PLX presented us with as interesting a set of issues regarding antitrust in high-tech markets as did Google – albeit in a somewhat more low-key atmosphere.

The issues raised by IDT/PLX spanned the Merger Guidelines.[5] In the interest of time and our HSR confidentiality provisions, I won't provide a full blown Merger Guidelines analysis

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[1] *See* Press Release, FTC Charges Deceptive Privacy Practices in Google's Rollout of Its Buzz Social Network (Mar. 30, 2011), *available at* http://www.ftc.gov/opa/2011/03/google.shtm.

[2] *See* Press Release, Google Will Pay $22.5 Million to Settle FTC Charges it Misrepresented Privacy Assurances to Users of Apple's Safari Internet Browser (Aug. 9, 2012), *available at* http://ftc.gov/opa/2012/08 /google.shtm.

[3] *See* Press Release, FTC Closes Investigation of Google AdMob Deal (May 21, 2010), *available at* http://ftc.gov/opa/2010/05/ggladmob.shtm.

[4] *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.

[5]. U. S. DEP'T OFJUSTICE & FED TRADE COMM'N, HORIZONTAL MERGER GUIDELINES (Aug. 19, 2010), *available at* http://www.ftc.gov/os/2010/08/100819hmg.pdf.

of the case. Instead, I will walk you through the issues of most interest to me – one of five Commissioners who happens to have a deep background in law enforcement and litigation – as I weighed the arguments for and against the merger. In so doing, I hope to give you as practitioners some useful insight into my enforcement philosophy as an FTC Commissioner generally, and my views on high-tech mergers in particular. I'll conclude with some generic lessons that I believe can be drawn from the IDT/PLX case for future reference.

In broad strokes, the issues I found to be of most interest were:

- First, what were customers – large and small – saying about the relevant antitrust market in which to analyze the effects of the merger? Relatedly, what were those customers telling us about the nature of competition in that relevant market? Were they concerned about price competition, or were there other dimensions of competition affected by the merger – in particular innovation and customer service – that mattered equally (or perhaps even more) to them than the antitrust Holy Grail otherwise known as price effects?

- Second, what did the parties' ordinary course documents tell us about the relevant market and competition in that market today?

- Third, what was the past evidence regarding entry and repositioning telling us about the likelihood of either happening in the post-merger world? If, as was argued, the market truly was at an inflection point or was threatened by technological leapfrogging, then I could think of no better yardstick than natural experiments that have already occurred to test these arguments.

This list is not exhaustive. Neither is it ranked in any particular priority. I happen to think it is very important in weighing whether to challenge a merger that we Commissioners look at the totality of the evidence, and the direction that evidence takes us, on balance.

2. The Transaction and Investigation

Before I get into the specifics of these issues, let me start with a few words about the companies involved. Unlike Google, neither IDT nor PLX is a household name, much less a verb. Nonetheless, both firms make a number of components that are essential to the computer hardware devices that we rely on every day, namely PCs, servers and data storage systems.

The principal overlap created by the merger was in PCIe switches. PCIe switches are integrated circuits – otherwise known as silicon chips – that play a vital role in computer architecture. Using the PCIe data transfer protocol, these switches create high-speed, point-to-point connections between multiple input/output devices and the microprocessor in a computer device. The PCIe protocol is one of several data transfer protocols used to transmit data packets. Other such protocols include SAS, Ethernet, InfiniBand, and Fibre Channel. These other data

transfer protocols were an important element in the debate about the relevant market affected by the merger, of which more in a moment.

IDT and PLX announced their intention to merge in April of last year. Had the merger proceeded, the merged firm's market share would have exceeded 80 percent of the worldwide PCIe switch market. The FTC issued Second Requests to the parties in July 2012. Between July and December 2012, FTC's Mergers II staff conducted a fast-paced, nimble, yet thorough investigation of the merger. The Commission determined it should block the merger. On December 18, staff filed a 13-page Part 3 complaint[6] outlining why the merger should be blocked. Two days later, on December 20, the parties abandoned the merger.

3. Issues

So let's now turn to three of the interesting aspects of this case – customer evidence; documentary and economic evidence; and natural experiments regarding entry.

From FTC staff's standpoint, the IDT/PLX transaction was a plain vanilla merger to near monopoly in PCIe switches, with a small but insignificant fringe. As one would expect to see with a merger to near monopoly, staff uncovered convincing evidence that the parties were each other's closest competitors, and that they competed with one another in a unique way along several dimensions, including price, innovation, and customer service. According to the complaint, the merger was therefore 'likely to substantially lessen competition for the development and sale of PCIe switches on a worldwide basis, leading to higher prices, lower quality, and less innovation.'[7]

From my standpoint, the complaint allegations regarding the relevant market and competition were well founded in real-world customer evidence. Within the confines of the HSR confidentiality provisions, I cannot describe all the arguments made by IDT, PLX, and their very able counsel in their white papers and discussions with Commissioners in defense of the merger. However, I can tell you that, during the pendency of the FTC review, PLX stated on a quarterly conference call with analysts that PCIe switches were not a relevant market.[8] Instead, PLX management argued, PCIe switches were part of a wider "systems interconnect solutions" market, in which PCIe competes with various data transfer protocols including Ethernet and InfiniBand, to name but two. PLX also told the analysts that their "main competitor" was Intel,[9]

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[6] *In the Matter of* Integrated Device Technology, Inc., a corporation, and PLX Technology, Inc., a corporation Docket No. 9354 FTC File No. 121 0140 *available at* http://www.ftc.gov/os/adjpro/d9354/121218 idtplxadmincmpt.pdf (Part 3 Complaint).

[7] *Id* ¶ 1.

[8] *PLX Technology, Inc.: Q3 2012 Earnings Call Transcript*, MORNINGSTAR (Oct. 29, 2012), http://www.morningstar.com/earnings/earnings-call-transcript.aspx?t=PLXT&qindex=2

[9] *Id*.

which has in recent years sought to include PCIe functionality in its CPUs, in some cases reducing customer reliance on standalone PCIe switches.

To be sure, we took these and other arguments regarding the relevant market and competition quite seriously. In interviews, staff carefully walked customers through PCIe competitive options available to them – including Intel and other data transfer protocols – focusing on the very important question of what customers *would* do if faced with a non-transitory price increase, as opposed to what they *could* do, and whether those options made economic sense. It is safe to say that the majority of customers interviewed by staff stated consistently that PCIe switches were a relevant market.

Perhaps unsurprisingly, customers were concerned about the competitive effects of the merger, not only on price, but also on innovation and customer service. These latter dimensions of competition are often overlooked in a fast-moving merger review, in my opinion. And yet they matter to high-tech customers – a lot.

In particular, with respect to innovation, there had been a protracted history of innovation competition between IDT and PLX, with each new switch generation forcing the other firm to add new and important features to its switches. Although price was not unimportant to customers, it frequently ranked below these innovations on a list of three or four variables taken into account in making their purchasing decisions.

Similarly, customer service and support was another critical competitive variable on an equal footing with price for most customers, as well as for the parties themselves. IDT and PLX provided sophisticated customer support throughout the PCIe switches' life cycle, and also worked with customers as they designed new computer architectures. In other words, I am not just talking about a 1-800 number that routes the customer query to a call center. This 'cradle to grave' customer service was a key competitive variable identified by customers that they believed would be negatively impacted by the merger. We were therefore concerned that, in the post-merger world, 'the resulting monopolist will have greater freedom to reduce the resources it allocates to customer support.'[10]

Let's turn to the documentary evidence. This documentary evidence told a story that was quite consistent with the customer evidence. A casual read of the complaint will tell you that there were more than a few hot documents found by staff during the investigation. IDT and PLX's senior management repeatedly identified each other as their primary competitor. One party document even described the merger as a "near monopoly."[11]

Turning to the third issue – namely entry and repositioning – this was another area in which listening hard to customers and a review of the documents proved to be very instructive. There is an adage in the tech procurement industry that 'no one ever got fired for buying IBM.' Well, the adage seems to hold true in many tech markets today, not just those in which IBM is a

[10] Part 3 Complaint, *supra* note 5, ¶ 30.

[11] *Id*. ¶ 2.

vendor. For customers, it was low risk to source from the established players in the market, namely IDT and PLX, and this was not just a matter of preference (as was found to be the case by Judge Walker in *PeopleSoft/Oracle*).[12] IDT and PLX had successfully developed a portfolio of reliable switch products that were backward compatible. It would simply not have been economical for customers to start over again with a new vendor, even at the pre-design phase before the PCI switch was baked-into a system.

4. Lessons

So what are the lessons here? Broadly speaking, I would break them down as follows:

First, the FTC can and does enforce the antitrust laws in fast-moving high-tech markets, even when faced with complex arguments about how a market might be at an inflection point – in this case Intel's move to place more PCIe functionality on its CPU - and a potential market shift to other data transfer protocols. When presented with arguments about 'technology leapfrogging' or 'market inflection points,' we will take these arguments seriously, to be sure. But don't be surprised if these arguments turn out to be nothing more than clichés when market tested in the real world.

Second, low-tech enforcement tools are useful in high-tech markets, as with any other market. Of course, robust data when available will be incorporated into our reviews; however, it is but one lens through which to look at a merger. Equally important are documents and customer evidence regarding the relevant market, existing competition, and entry and repositioning. These low-tech tools are supple enough and equal to the task of informing decisions in high-tech markets as they are in rust belt markets. As two distinguished lawyers from Skadden recently commented: "Rather than pose the quixotic question of what economic theory or model most accurately predicts competitive effects, the antitrust policy makers and decision makers should re-emphasize the importance of the careful application of good judgment, and attention to details about marketplace dynamics in resolving antitrust disputes. After all, the best way to predict what will happen in the real world is to consider every available piece of evidence – quantitative or not – about what happens in the real world."[13]

I couldn't agree more.

Finally, in high-tech markets the impact a merger may have on non-price competition matters – a lot. Price matters, to be sure, but it can rank behind innovation competition, as well as customer service.

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

[13] Shepherd Goldfein & Neal R. Stoll, *Back to Basics: the (Over)Use of Economic Models in Antitrust,* N.Y. L.J. (July 10, 2012), *available at* http://www.skadden.com/sites/default/files/publications/NYLJ_Back_to_Basics_July_2012.pdf.

So thanks so much again for inviting me to come speak to you all today. I look forward to the panel discussion on these issues.