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The Proper Role of Privacy in Merger Review

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I. INTRODUCTION

There have been increasing calls for the Federal Trade Commission (“FTC”) and U.S. Department of Justice (“DOJ”) to consider the potential loss of consumer privacy as a factor in their merger reviews and to challenge mergers of firms with large stores of personal data that otherwise pose no apparent competitive issues.² These calls are unlikely to be successful. Standalone privacy concerns cannot be factored into the merger review process in a way that is consistent with the antitrust statutes and existing precedent. There are also good policy reasons against incorporating traditional privacy concerns into antitrust doctrine.

Nevertheless, in industries where firms differentiate themselves through their approaches to privacy, a merger could reduce the incentive of a merged entity to compete on this basis. A substantial lessening of this competition could be a basis on which to block a proposed transaction. Still, the number of transactions that will raise serious concerns about loss of privacy competition is likely to be very limited even in digital markets.

II. IS PRIVACY A RELEVANT CONSIDERATION IN COMPETITION LAW?

There remain many unanswered questions about the scope of the Sherman and Clayton Acts, but whether these statutes reach consumer protection concerns such as privacy is not one of them. The U.S. Supreme Court has made clear on numerous occasions that non-competition factors cannot be considered in antitrust analysis. The Court has explained that antitrust law is concerned with fostering vigorous competition, on the view that this will lead not only to the lowest prices, but also to the highest quality products and the greatest degree of innovation.

As far back as 1931, the Supreme Court held that standalone consumer protection concerns may not be addressed using competition law.³ In *FTC v. Raladam Co.*,⁴ the Court held that a company’s deceptive advertisements for an obesity cure were beyond the FTC’s “unfair methods of competition” jurisdiction unless the FTC could show that there was a reduction in competition. This decision led Congress to pass the 1938 Wheeler-Lea Amendments to the FTC Act, which expanded the FTC’s jurisdiction to include “unfair or deceptive acts or practices.”⁵

In a series of subsequent decisions, the Court reaffirmed that competition is the lodestar of antitrust analysis and that courts may not consider other factors. For example, in *United States*

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² See, e.g., Comments of the Electronic Privacy Information Center (EPIC) to FTC Remedy Study (Mar. 17, 2015), available at <https://epic.org/privacy/internet/ftc/Merger-Remedy-3-17.pdf>.

³ For a history of privacy enforcement and its relationship with antitrust doctrine, see Maureen K. Ohlhausen & Alexander Okuliar, *Competition, Consumer Protection, and the Right (Approach) to Privacy*, 80 ANTITRUST L.J. ___ (forthcoming 2015).

⁴ 283 U.S. 643 (1931).

⁵ Act of Mar. 21, 1938, ch. 49, § 3, Stat. 111 (codified at 15 U.S.C. § 45(a)).

v. Philadelphia National Bank,⁶ the Court held that the effect upon competition is the sole criterion to determine whether a merger violates Section 7 and that consideration of other social or economic factors (there, the prospect of bringing more jobs to the merged entity's home city) was improper.⁷

Given the text of the antitrust statutes, no other result would be justified. Section 7 of the Clayton Act requires a showing that the effect of an "acquisition may be substantially to lessen competition," Sections 1 and 3 of the Sherman Act require a restraint of trade, and Section 2 of the Sherman Act requires an act of monopolization. These requirements, all of which reflect a goal of unfettered competition, do not lend themselves to the protection of interests such as privacy.

The antitrust agencies have likewise explained that antitrust law is only concerned with competitive effects. The 2010 Merger Guidelines state that the only consideration in merger analysis is whether a transaction "may substantially lessen competition."⁸ The words "privacy" and "data protection" do not appear anywhere in the Guidelines. The FTC explicitly rejected calls to consider privacy in competition analysis in *Google/DoubleClick* and did so implicitly in *Facebook/WhatsApp* as well.⁹

This judicial and agency restraint rests on firm policy grounds. For one thing, privacy is difficult to quantify compared to traditional antitrust factors like price and output. How would one determine the effect on consumer welfare from a change in a company's privacy policy or data security practices? This concern is compounded by the variety of concepts of privacy. In addition, consumers have mixed views about the optimum level of privacy. Unlike lower prices, which can be observed and which consumers universally value, the concept of "more" or "better" privacy is not always clear and consumers value privacy in different ways, with some viewing it as a detriment.¹⁰

In a law enforcement system based on both antitrust and privacy considerations (or other non-competition considerations), there will be frequent tensions between the two modes of analysis. For example, aggregation of personal data from a corporate acquisition might raise concerns about greater privacy intrusions, but the antitrust laws would view this aspect of the

⁶ 374 U.S. 321, 371 (1963) (holding that a merger that substantially reduces competition "is not saved because, on some ultimate reckoning of social or economic debits and credits, it may be deemed beneficial").

⁷ See also *N.C. State Bd. of Dental Exam'rs v. FTC*, 135 S. Ct. 1101, 1109 (2015) (stating that the antitrust laws are intended "to promote robust competition;" lower court affirmed the FTC's rejection of non-competition defenses); *FTC v. Ind. Fed'n of Dentists*, 476 U.S. 447, 463 (1986) (health and safety defense asserted by dentists refusing to provide x-rays to insurance companies is "nothing less than a frontal assault on the basic policy of the Sherman Act"); *United States v. Nat'l Soc'y of Prof'l Eng'rs*, 435 U.S. 679, 690 (1978) (the rule of reason inquiry under the Sherman Act "is confined to a consideration of impact on competitive conditions").

⁸ U.S. Dep't of Justice & Fed. Trade Comm'n, Horizontal Merger Guidelines § 1 (2010) [hereinafter Merger Guidelines], available at <http://www.ftc.gov/os/2010/08/100819hmg.pdf>.

⁹ The European Court of Justice and European Commission likewise rejected calls to consider privacy in competition matters in *Asnef-Equifax v Asociación de Usuarios de Servicios Bancarios (Ausbanc)* and *Facebook/WhatsApp*, respectively.

¹⁰ Witness the millions of people that have public Facebook profiles and the many others who seek to maximize the number of followers on their Twitter or other social media sites.

combination as a potential efficiency due to the potential for lower costs and development of better services. Without a clear standard for how to weigh the competition versus the privacy considerations, the outcome is likely to reflect the personal views of the particular enforcer reviewing the transaction, ultimately leading to less predictability and less consistency in outcomes.

An additional concern is that competition remedies are not well suited to address privacy concerns. As the FTC pointed out in its *Google/DoubleClick* closing statement,¹¹ privacy enforcement through merger control may result in uneven privacy restrictions on market participants, which could have an adverse effect on competition. In particular, firms that are able to collect significant amounts of personal data unilaterally would have a competitive advantage against firms that seek to obtain similar data sets through acquisition. This might advantage large, vertically integrated incumbents against smaller rivals and new entrants.

Finally, it is unclear what shortcoming of consumer protection enforcement exists that would justify the need for expanding antitrust's reach. The FTC and state attorneys general have a long history of protecting consumer privacy through their consumer protection authority, and the Consumer Financial Protection Bureau has joined these efforts in the financial sector. These enforcers, supplemented by appropriate private enforcement, already have the necessary tools to address concerns about consumer harm from mistreatment of personal data.

III. IS PRIVACY A FORM OF NON-PRICE COMPETITION COGNIZABLE BY THE ANTITRUST LAWS?

In most industries, firms compete to sell their goods or services on the basis of price, features, and distribution, among other dimensions. In some markets, these other dimensions include competition on the basis of their privacy or data security protections.¹² A company may seek to gain users by advertising that it collects no personal information or that it encrypts communications with its users, for example. In theory, a merger between firms that are close competitors on the basis of their privacy protections could lead to anticompetitive effects, in much the same way that a merger between two firms that are close competitors on the basis of their product features could lead to anticompetitive effects.

In recognition of this, the antitrust agencies consider the potential loss of privacy competition in the course of their merger reviews. In the *Google/DoubleClick* investigation, the FTC considered whether the “transaction could adversely affect non-price attributes of competition, such as consumer privacy.”¹³ Several FTC officials have recently stated that the agency is paying attention to privacy competition in merger investigations. In addition, the 2010 Merger Guidelines place greater emphasis on the role of non-price competition.

Despite what appears to be a widespread recognition that privacy can be a form of non-price competition cognizable under the Merger Guidelines, there does not appear to be any

¹¹ Statement of Fed. Trade Comm'n at 2, *Google/DoubleClick*, FTC File No. 071-0170 (Dec. 20, 2007), available at http://www.ftc.gov/system/files/documents/public_statements/418081/071220googledc-commstmt.pdf.

¹² Although privacy and data security are distinct concepts, for simplicity I refer to both as “privacy” for the remainder of the article.

¹³ *Google/DoubleClick* Statement, *supra* note 11, at 2-3.

generally accepted means of assessing which transactions will lead to anticompetitive effects due to a loss of privacy competition. This may be due in part to the lack of empirical evidence indicating that a larger firm would treat consumer privacy less favorably than a smaller firm. There is at least some (admittedly mixed) empirical evidence suggesting that higher concentration levels are correlated with higher prices. However, neither economic theory nor empirical evidence suggests a consistent relationship between industry concentration and the degree of privacy protection offered (or even product quality generally).¹⁴

To the extent there is a link between concentration and privacy, it may well be a positive relationship, i.e., larger firms may tend to protect privacy better than smaller firms. A firm that reduced its privacy protections to collect more data would be marginally adding to its costs for the purpose of delivering a better product—hardly the type of conduct we would expect from a firm with substantial market power.¹⁵ In addition, larger firms are under greater scrutiny by the press, consumers, and regulators. Data breaches, changes in privacy policies, and enforcement actions against larger firms are widely reported in the press. In addition, larger firms have more resources to devote to data security and privacy.

Nevertheless, one could apply a standard Merger Guidelines unilateral effects analysis to evaluate the loss of privacy protection from a proposed merger or acquisition. Under this approach, potential concerns may arise when each of the following elements are met in addition to satisfying the standard structural case:¹⁶

- The merging firms are significant rivals due to their competition on privacy;
- A large share of customers regard the merging parties as offering the best products as a result of their approaches to privacy; and
- Rivals must be unlikely to revise their approach to privacy to better compete with the merged firm (i.e., no repositioning).

As part of the assessment of competitive effects, the reviewer would also consider other standard Merger Guideline factors such as entry, efficiencies, and the failing firm defense. A benefit to this approach is that there is no need to quantify the strength of a company's privacy offerings or determine the "optimum" level of privacy for consumers in the industry or even any particular segment of consumers. All that matters is that a substantial number of consumers view the merging parties as offering the best services specifically because of their privacy policies. When these conditions hold, the merged company will be able to successfully exercise market power because few of its customers will defect to other suppliers.

¹⁴ OECD, *The Role and Measurement of Quality in Competition Analysis* 7 (2013) ("The empirical evidence that is available suggests that increasing competition can have either positive or negative effects on quality levels, depending on the particular market circumstances.").

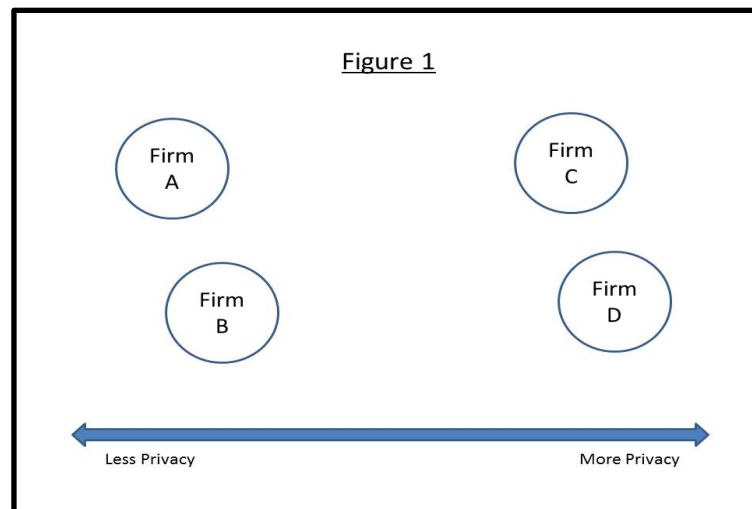
¹⁵ James C. Cooper, *Privacy and Antitrust: Underpants Gnomes, The First Amendment, and Subjectivity*, 20 GEO. MASON L. REV. 1129, 1135-36 (2013).

¹⁶ FTC Commissioner Julie Brill has proposed a similar inquiry. See Julie Brill, Comm'r, Fed. Trade Comm'n, *Weaving a Tapestry to Protect Privacy and Competition in the Age of Big Data* 7 (June 2, 2014), available at https://www.ftc.gov/system/files/documents/public_statements/313311/140602edpsbrill2.pdf.

Another benefit to this approach is that it will not condemn any transactions beyond the standard unilateral effects test in the Merger Guidelines. By employing a similar approach as Section 6.1 of the Merger Guidelines, the three-part test allows a reviewer to isolate the source of the unilateral effects as coming from privacy competition, as opposed to some other form of competition (e.g., product features, quality). The risk of Type 1 error, which is likely to be high when dealing with an abstract concept such as privacy competition, should accordingly be minimized.

One takeaway from this test is that even in a market where firms compete on the basis of privacy, unilateral effects are unlikely unless the merger is between two firms with strong privacy protections. Transactions such as *Facebook/WhatsApp*—where the concern was that Facebook might revise WhatsApp’s more consumer-friendly privacy policy and apply Facebook’s policy—are the least likely to raise unilateral effects concerns regarding loss of privacy competition. Instead, a merger between firms that both offer greater privacy protections than other market participants is far more likely to lead to anticompetitive privacy effects.

For example, assume Firms A, B, C, and D are competing social networks and that consumers select their provider based on a number of considerations. For some consumers, the decision of which provider to use is driven largely by the providers’ privacy protections. Firms A and B offer relatively limited privacy protections, while Firms C and D offer greater privacy protections. As a result, Firms C and D attract many of their users due to their favorable privacy policies. This is illustrated in Figure 1.



If Firm A were to acquire Firm C, it is unlikely that Firm A would revise Firm C’s approach to privacy to be less consumer friendly. If it did, many of Firm C’s users would switch to Firm D, making the privacy change unprofitable.

In contrast, if Firms C and D were to merge, they could revise either or both of their approaches to privacy to be less consumer-friendly while losing little overall business.¹⁷ So long as Firms C and D continue to offer better privacy protections than Firms A and B, few customers of Firms C and D will defect and a reduction in privacy will be profitable.

Notice that the strength of these results depends on how many of Firm C and D's customers selected those firms based on their privacy policies. The less significant the role of privacy in consumers' choice of providers, the less significant are the unilateral effects from a merger between Firms C and D because more users of C and D will be willing to switch to A or B.

Likewise, these results also depend on Firms C and D offering significantly better privacy protections than most other industry participants. If all four firms offered comparable privacy protections, many users of C and D's services would switch to A or B, making a diminution of privacy unprofitable.

In other words, unilateral privacy effects are only likely to arise where privacy is an important element of competition and the merger is between two firms that offer stronger privacy protections than most other rivals. These are necessary, but not sufficient, conditions for unilateral effects to arise. As noted above, a merger that satisfied the three-part test would pose no problems if there were *de novo* entry, significant merger-specific efficiencies, or other successful defenses.¹⁸

Another, potentially counterintuitive takeaway is that the injury to consumers from a loss of privacy competition is not necessarily less privacy. To be sure, a company acquiring a close competitor on the basis of privacy could exercise its newfound market power by reducing its privacy protections. But far more likely, it would simply increase prices or, in a market with zero prices, reduce investment in its services. According to FTC guidance, companies must take certain potentially unattractive steps before weakening their privacy policies,¹⁹ whereas a price increase or reduction in investment could be implemented immediately and with no specific regulatory oversight.

In sum, privacy as an element of competition will be a relevant consideration in very few merger reviews, which may explain why no case has been brought along these lines. For the rare merger that presents a genuine risk of loss of privacy competition, the most likely harm to consumers would be fairly ordinary: higher prices or lower quality of services, not diminished privacy protections.

¹⁷ Here I assume that the merging firms would have an incentive to reduce privacy protections to collect more user data, thereby generating greater revenue. As noted in the main text, there are reasons to question the accuracy of this assumption.

¹⁸ As evidenced by the Facebook/WhatsApp transaction, consumers with strong privacy preferences may switch to upstart competitors in large numbers if there are concerns that a transaction will lead to a reduction in privacy. See Case COMP/M.7217—*Facebook/WhatsApp*, Comm'n Decision, ¶ 174 (Mar. 10, 2014) (“Privacy concerns also seem to have prompted a high number of German users to switch from WhatsApp to Threema in the 24 hours following the announcement of Facebook’s acquisition of WhatsApp.”).

¹⁹ FTC Blog, *Mergers and Privacy Promises*, Mar. 25, 2015, <https://www.ftc.gov/news-events/blogs/business-blog/2015/03/mergers-privacy-promises>.