

# BLIND ORACLE: THE FLAWED ROLE OF POTENTIAL ENTRY IN *UNITED STATES v.* *ORACLE* AND A PROPOSAL FOR CHANGE

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## INTRODUCTION

On September 9th, 2004, a Northern District of California court dealt a surprising blow to the Antitrust Division of the U.S. Department of Justice (DOJ or Division).<sup>1</sup> On that day, Judge Vaughn R. Walker rejected the DOJ's attempt to block the merger of Oracle Corporation (Oracle) and PeopleSoft, Inc. (PeopleSoft).<sup>2</sup> The decision marked a turning point not only for the parties themselves, but also for the Division and its efforts to ensure the preservation of the competitive markets that protect consumers.<sup>3</sup>

The most damaging aspect of the court's decision is not necessarily the outcome of the case itself and its impact on consumers. Nor is it the federal government's uncharacteristic defeat. What is significant is the manner in which Judge Walker reached his decision and the detrimental effect it has had on merger enforcement ever since. Rather than focus on the possible anticompetitive effects that could result from the proposed merger, Judge Walker centered his opinion on the definition of the market that would be impacted by the transaction. In so doing, he placed tremendous weight on one of the most nebulous factors to be considered in merger analysis: potential entry. The court held that the possible entry of both outsourcing options and Microsoft into the merging parties' core area of competition indicated that the government had defined the product market too narrowly and should have included these additional potential competitors into its definition.<sup>4</sup> Because the government had failed to meet its burden to properly define the product market, the court would not analyze in

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1. *United States v. Oracle Corp.*, 331 F. Supp. 2d 1098 (N.D. Cal. 2004); see also Steve Lohr & Laurie J. Flynn, *Judge Allows Oracle to Bid for PeopleSoft*, N.Y. TIMES, Sept. 10, 2004, at C1.

2. *Oracle*, 331 F. Supp. 2d at 1101.

3. Jason McClure, *Gun Shy? Antitrust Division Chief Defends Enforcement Record*, NEW YORK LAW JOURNAL, Jan. 11, 2007, at 2.

4. *Oracle*, 331 F. Supp. 2d at 1159–60.

detail the likely impact on competition. The inquiry into the anticompetitive effects of the merger ended before it had even begun.

This decision reflects the law's unsettled and unbalanced treatment of potential entry in horizontal merger challenges. Whereas traditional potential competition doctrine has imposed significant burdens of proof on plaintiffs establishing the importance of potential entrants on future competition, the law has not required the same of defendants.<sup>5</sup> The *Oracle* decision marks what could be considered a high-water mark for this legal disparity, and has left an unfortunately lasting impact on merger enforcement.

In this Note, I will argue that *Oracle* gave too much weight to the theory of potential entry by evaluating the existence of potential entrants at the market definition phase of the merger analysis without requiring the defendant to offer specific evidence showing that those actors were likely to enter successfully. Rather than examine potential competitors to define the product market, a better system would evaluate such actors for their effect on post-merger competition. Moreover, the court would only evaluate these potential competitors after the parties had established their relevance by convincing proof, perhaps following the example suggested by the DOJ's Horizontal Merger Guidelines (Guidelines).

Part I of this Note will discuss the role of potential entrants in horizontal merger analysis both under the Guidelines and in court analysis, and will show how the treatment of such actors differs according to whether they are introduced by plaintiffs or by defendants. Part II will address the *Oracle* case, paying particular attention to the court's focus on potential entry as the basis for expanding the proposed product market. Part III will argue that the rationale behind Judge Walker's decision was flawed in its cursory analysis of so erratic an actor as the potential entrant, and is indicative of the law's unbalanced treatment of potential entry for plaintiffs and defendants. Part IV will address the post-*Oracle* landscape of merger enforcement. Finally, Part V will propose a system for analyzing potential competition that more fairly treats plaintiffs and defendants without giving as much power to so uncertain an actor as the potential entrant.

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5. Darren Bush & Salvatore Massa, *Rethinking the Potential Competition Doctrine*, 2004 Wis. L. REV. 1035, 1076 (2004).

## I.

## POTENTIAL ENTRANTS IN HORIZONTAL MERGER ANALYSIS

Antitrust law currently treats potential entrants differently depending on which party presents the information.<sup>6</sup> While the DOJ uses specific ground rules for evaluating potential entrants and their impact on competition,<sup>7</sup> courts vary greatly in their analysis. Courts require substantial and specific evidence from plaintiffs who argue that potential entrants are relevant to a product market,<sup>8</sup> while courts will accept more cursory suggestions of potential entry by defendants.<sup>9</sup>

A. *Potential Entry Under the DOJ Horizontal Merger Guidelines*

The Antitrust Division of the DOJ is tasked with protecting the competitive process, the economy, and consumers themselves, through the enforcement of the antitrust laws.<sup>10</sup> These laws rest on the theory that competition protects economic freedom by ensuring lower prices, better quality, and more choice for American consumers.<sup>11</sup> Section 7 of the Clayton Act prohibits one party engaged in commerce from acquiring the assets of another party engaged in commerce if “the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly.”<sup>12</sup> As a result, the DOJ evaluates proposed mergers and acquisitions to be sure that they will not unduly increase the merged party’s market power and thus limit or hinder competition in the market place.<sup>13</sup>

In making these decisions, Division attorneys look to the Horizontal Merger Guidelines issued in 1992 by the DOJ and Federal Trade Commission.<sup>14</sup> The Guidelines set forth the analytical framework that the antitrust agency should apply when deciding whether a proposed merger is likely to pose anticompetitive concerns.<sup>15</sup> The Guidelines propose two main theories under which the Division can allege that the merger will harm competition. Under the “coordinated

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6. *Id.* at 1128.

7. U.S. DEP’T OF JUSTICE & FED. TRADE COMM’N, HORIZONTAL MERGER GUIDELINES §§ 1.3, 3 (1992) [hereinafter GUIDELINES].

8. *See* Bush & Massa, *supra* note 5, at 1128.

9. *Id.* at 1076.

10. Antitrust Division Overview, <http://www.usdoj.gov/atr/overview.html> (last visited Sep. 18, 2009).

11. *Id.*

12. 15 U.S.C. § 18 (2006).

13. GUIDELINES, *supra* note 7, § 0.1.

14. *Id.* § 0.2.

15. *Id.* § 0.1.

effects theory,” the merger is deemed to harm competition if it threatens to make anticompetitive coordinated action by the remaining firms in the market easier and more likely.<sup>16</sup> The “unilateral effects theory,” which the DOJ employed in *Oracle*, states that a merger harms competition if it allows the combined entity to profitably raise prices and suppress output following the merger, thus hurting consumers.<sup>17</sup> While before the merger such anticompetitive action would not have been economically feasible for the company acting alone, the additional market power gained by the merger can make such behavior profitable to the company.<sup>18</sup>

Both theories require the Division to first define the relevant product market.<sup>19</sup> To define a market, the Guidelines and relevant case law evaluate possible consumer responses to a price increase imposed by a hypothetical monopolist.<sup>20</sup> If this theoretical monopolist could profitably impose a “small but significant and nontransitory” increase in price (SSNIP) on a group of products, then the analysis looks to how consumers would react to such a price increase. If there are functionally interchangeable products to which consumers would switch rather than continue to use the now more expensive product made by the monopolist, then the market must include those substitute products. The larger the market, the less likely it is that the SSNIP will be profitable, making anticompetitive conduct by the merged parties less likely.

Market definition thus acts as a threshold matter for merger challenges for two reasons. First, a large market presupposes that the merged entity is unlikely to raise prices in an anticompetitive manner. Second, even if the merged entity does raise prices, there will at a minimum be enough additional options that consumers will not experience any negative impact by such a change.<sup>21</sup> The finding of a broad product market therefore makes a merger challenge arguably unnecessary, or at least unsuccessful.

The Guidelines address potential entry in two different ways. First, the Division can decide to include a potential entrant among the relevant product market’s participants.<sup>22</sup> The Division will include this “uncommitted entrant” in the market definition if the entrant’s

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16. *Id.* § 2.1.

17. *Id.* § 2.2.

18. *Id.* § 2.21.

19. *United States v. Oracle Corp.*, 331 F. Supp. 2d 1098, 1110 (N.D. Cal. 2004).

20. *Id.* at 1111–12; *see also* GUIDELINES, *supra* note 7, §§ 1.11, 1.21.

21. *Oracle*, 331 F. Supp. 2d at 1112.

22. GUIDELINES, *supra* note 7, § 1.0.

response to a SSNIP would be to “enter rapidly into production or sale of a market product in the market’s area, without incurring significant sunk costs of entry and exit.”<sup>23</sup> To qualify, firms must be able and likely to shift existing assets into the market within one year.<sup>24</sup> The Guidelines instruct the Division to consider costs of substitution for consumers, whether the firm’s assets and capacity are already over-extended, and its ability to respond to an increase in price.<sup>25</sup>

Additionally, the DOJ may evaluate a potential entrant as a possible mitigating factor to the anticompetitive effects posed by a merger. The Guidelines state that if entering the product market is so easy that the merged party could no longer profitably maintain a SSNIP, then the merger is unlikely to pose a competitive threat and the Division need not challenge the transaction.<sup>26</sup> Again, the Guidelines require that the potential entrants satisfy specific criteria to fall within this category. Entry must not just be possible, but rather must be “easy,” which is defined as “timely, likely, and sufficient in its magnitude, character and scope to deter or counteract the competitive effects of concern.”<sup>27</sup> The timeliness criterion is generally met by entry within two years.<sup>28</sup> The government may show that entry is likely if the entrant would find the move profitable, would be able to achieve minimum viable scale in its new endeavor, has sufficient sales opportunities in the market, and would be able to divert sales from the incumbent firms.<sup>29</sup> Sufficiency is established by showing that the magnitude, character, and scope of entry would deter or counteract the competitive effects at issue, either through availability of essential assets, or through responsiveness to localized sales opportunities and demands.<sup>30</sup>

#### *B. Potential Entry for Plaintiffs: Potential Competition Doctrine*

As the plaintiff in merger challenges, the government may introduce potential entry as the basis of suit. In these cases, the DOJ typically takes the position that a proposed acquisition of a company that is not yet in the market would have entered the market as a competitor but for the merger.<sup>31</sup> Plaintiffs must clear high evidentiary hurdles

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23. *Id.*

24. *Id.* § 1.321.

25. *Id.*

26. *Id.* § 3.0.

27. *Id.*

28. *Id.* § 3.2.

29. *Id.* § 3.3.

30. *Id.* § 3.4.

31. Bush & Massa, *supra* note 5, at 1043.

before advancing such a claim. In *United States v. Marine Bancorp.*,<sup>32</sup> the Supreme Court required the government plaintiff to show that the potential entrant would have had a significant pro-competitive effect on the market had the merger not occurred.<sup>33</sup> Such a showing requires substantial and specific evidentiary support that is difficult to obtain,<sup>34</sup> making this an uncommon posture for the DOJ to pursue.

Lower courts have followed *Marine Bancorp.* to enforce similarly exacting evidentiary standards from plaintiffs challenging mergers based on potential entry.<sup>35</sup> These courts have required heightened standards of proof to establish the presence of potential entrants and the likelihood of entry, including “clear proof,” “reasonable probability” that the party “would likely” enter the market, and that the party had the “intent and ability” to enter said market.<sup>36</sup> These standards reflect efforts by the courts to ensure, to the extent possible, that the DOJ is correct in its assessment of potential entry; courts are hesitant to grant judicial approval before they are convinced that the alleged potential entrant will actually enter and compete in the market as the plaintiff says it will.

### C. *Potential Entry for Defendants: Potential Competition as a Defense*

Antitrust defendants may use potential entrants to their own advantage in a number of ways. Traditionally, the defendant argues that the threat of entry operates as a continuing constraint on prices,<sup>37</sup> or that a certain company will enter the market in the near future and destroy any theoretical price increase the merged entity might have imposed.<sup>38</sup> Yet another approach is that taken by Oracle, in which the defendant invokes potential entry to refute the plaintiff’s proposed definition of the market.<sup>39</sup> This technique, in which potential entrants are used to enlarge the relevant product market, represents an expansion of the existing doctrine,<sup>40</sup> allowing the defendant to shift the

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32. 418 U.S. 602 (1974).

33. Bush & Massa, *supra* note 5, at 1057.

34. *See id.*

35. *See id.* at 1058–69 (discussing several circuit and district court approaches to potential entry claims made by the government).

36. *Id.* at 1128.

37. John E. Kwoka, *Non-Incumbent Competition: Mergers Involving Constraining and Prospective Competitors*, 52 CASE W. RES. L. REV. 173, 174 (2001).

38. Bush & Massa, *supra* note 5 at 1044.

39. *Id.* at 1074 (noting that this procedural posture in Section 7 claims did not emerge until the 1990s and thus far has only been directly addressed by lower courts).

40. *Id.* at 1074 n.287.

court's focus away from the anticompetitive effects of the merger, where it more rightfully belongs.

Courts vary in the standards of proof they require from defendants who are making potential entry arguments. In *United States v. Baker-Hughes*,<sup>41</sup> then-Judge Clarence Thomas, writing for the D.C. Circuit, acknowledged only a very low standard for defendants. Finding that "a defendant cannot realistically be expected to prove that new competitors will 'quickly' or 'effectively' enter" the market, he held that a defendant need only point to a firm that could *conceivably* enter the market.<sup>42</sup> Once a defendant clears this low threshold, the court does not have to examine whether the entry is likely to occur or what effect it might have on the behavior of the merged firm.<sup>43</sup>

The Districts of Delaware and Western Wisconsin have taken more moderate approaches. In *United States v. United Tote*<sup>44</sup> and *United States v. Franklin Electric*,<sup>45</sup> the courts undertook more fact-intensive inquiries into the following factors to determine the likelihood of future entry: incentives to enter, likelihood of successful entry, timeliness of entry, past failed attempts at entry by the entrant, possible customer responses, efforts of other players to enter the market, and the effect of having the entrant on the fringe of the market.<sup>46</sup> This approach more closely resembles the potential entry doctrine for plaintiffs (and the DOJ Guidelines themselves) in its reliance on evidence. Unfortunately, these decisions have little authority outside their own districts, making the lenient *Baker-Hughes* opinion the more popular reference for antitrust litigants.<sup>47</sup>

## II.

### *UNITED STATES V. ORACLE CORP.*

The *Oracle* debacle began when the Antitrust Division of the DOJ sought to block Oracle's \$7.7 billion takeover of PeopleSoft in

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41. 908 F.2d 981 (1990).

42. See Bush & Massa, *supra* note 5, at 1076. Ironically, the standard that Judge Thomas found so ridiculous in *Baker-Hughes* is precisely the standard that courts expect plaintiffs to satisfy in the same circumstances. See *id.* at 1128; see also *supra* Part I.B and accompanying notes.

43. Bush & Massa, *supra* note 5, at 1076.

44. 768 F. Supp. 1064 (D. Del. 1991).

45. 130 F. Supp. 2d 1025 (W.D. Wis. 2000).

46. Bush & Massa, *supra* note 5, at 1079.

47. See, e.g., Defendant Oracle Corporation's Trial Memorandum at 14, *United States v. Oracle Corp.*, 331 F.Supp. 2d 1098 (N.D. Cal. 2004) (No. C 04-0807); Plaintiff's Trial Brief at 28, *United States v. Oracle Corp.*, 331 F.Supp. 2d 1098 (N.D. Cal. 2004) (No. C 04-0807).

order to prevent its violation of Section 7 of the Clayton Act.<sup>48</sup> The government argued that the combination of the second and third largest players in their particular niche of the enterprise resource planning system software market would harm consumers by lessening the competition that typically keeps prices down.<sup>49</sup> Rather than object to the contention that the merger would yield anticompetitive effects, Oracle instead argued that the government's market definition was artificially narrow.<sup>50</sup> The court ultimately rejected the government's proposed market definition, which in turn prevented it from continuing into a more detailed statistical analysis of market power that would have required further proof from the defense. As a result, the court entered judgment for Oracle.<sup>51</sup>

### A. *The Parties*

Oracle and PeopleSoft develop, produce, market, and service enterprise resource planning (ERP) system software.<sup>52</sup> This kind of software integrates most of an organization's data across all or most of its activities, allowing a single software package to handle processing of systems for human resources management (HRM), financial management systems (FMS), customer relations, supply chain management, business intelligence, and others.<sup>53</sup> Oracle and PeopleSoft license these software programs to end user companies in packages that include maintenance and sometimes training.<sup>54</sup> Licensing and maintenance fees comprise only a small portion of the customer's expense (ten to fifteen percent), while extensive installation that includes training, consulting services, and integration with legacy systems makes up the bulk of the client's costs.<sup>55</sup>

The government confined its claims to "high function HRM software" and "high function FMS software," defining "high function"

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48. See Complaint at 4, *United States v. Oracle Corp.*, 331 F. Supp. 2d 1098 (N.D. Cal. 2004) (No. C 04-0807); Lohr & Flynn, *supra* note 1, at C1.

49. Complaint at 4, *supra* note 48. An interesting question not directly pertinent to this discussion is whether the court and DOJ should have considered the structure of the transaction as part of this antitrust inquiry. The proposed merger in question was the result of four unsuccessful hostile takeover bids by Oracle, each of which PeopleSoft vigorously rejected. PeopleSoft insisted that Oracle's overtures were a naked attempt to punish a successful competitor by driving away its customers through a lengthy takeover battle. Lohr & Flynn, *supra* note 1.

50. See *Oracle*, 331 F. Supp. 2d at 1148.

51. See *id.* at 1161.

52. *Id.* at 1101.

53. *Id.*

54. *Id.*

55. *Id.*

as only those “large complex enterprises” with the most complicated, extensive, “high functional needs.”<sup>56</sup> The government excluded from this category all “mid-market” producers of software that serve primarily mid-sized companies with less complicated software needs.<sup>57</sup> The government claimed that only Oracle, PeopleSoft, and Germany-based SAP AG were capable of producing these products.<sup>58</sup> The government argued that the merger would thus join two major players in a very small market, making a unilateral anticompetitive price increase a dangerous possibility.<sup>59</sup>

In turn, Oracle argued that the government had defined the market too narrowly. Oracle sought to include mid-market vendors capable of meeting up-market demands, third-party outsourcing options, “best of breed” vendors that sell only single product lines rather than the complete suite offered by Oracle and PeopleSoft, and incumbent legacy systems already in use by potential customers.<sup>60</sup> Oracle argued that the acquisition was necessary to effectively compete against Microsoft, which supposedly had plans to enter this up-market arena.<sup>61</sup> Furthermore, Oracle claimed that the high rate of innovation in the information technology industry prevented market boundaries from ever solidifying, thus making the DOJ’s market definition inaccurate.<sup>62</sup>

### B. *The Court’s Analysis*

The court ultimately found that the government had failed to meet its burden to properly define the relevant product market.<sup>63</sup> Noting that the term “high function software” does not exist independently in the industry but was rather created by the government for the purpose of litigation, the court found the characteristics of the proposed market too vague to meet the Section 7 requirement of a “well-defined” product market.<sup>64</sup> The court’s decision to dismiss all the customer testimony offered by the plaintiffs, finding it to be unpersuasive,<sup>65</sup> gravely damaged the government’s case. Judge Walker

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56. *Id.* at 1102–03.

57. *Id.* at 1102.

58. *Id.* at 1107.

59. *Id.*

60. *Id.* at 1149–58.

61. Lohr & Flynn, *supra* note 1.

62. Defendant Oracle Corporation’s Trial Memorandum, *supra* note 47, at 7. Not mincing words, Oracle called the DOJ’s definition “the most confusing, meaningless market definition ever pursued in a government merger challenge.” *Id.*

63. *Oracle*, 331 F.Supp.2d at 1161.

64. *Id.* at 1121.

65. *Id.* at 1130–32.

discounted the government's case further by choosing to reject its expert witness testimony for lack of a "quantitative metric," stating that "more is required" to establish a market in this kind of case.<sup>66</sup> As a result, the court found that the market must include several additional actors: outsourcing solutions, mid-market vendors, best of breed solutions, and Microsoft.<sup>67</sup> Given the number of market participants, the court refused to find a presumption of anticompetitive effects.<sup>68</sup>

The court's opinion indicates that it placed substantial reliance on the potential entry into competition of outsourcing service providers and Microsoft. The court found that most outsourcers have, or soon would have, blanket contracts or one-to-many business models in which the HRM provider contracts with the outsourcer, as opposed to contracting directly with the end user.<sup>69</sup> The court was particularly persuaded by the testimony of the outsourcing service provider Accenture, which claimed to have plans to adopt a one-to-many model within two years.<sup>70</sup> Previously, end users contracted directly with the HRM provider, using the outsourcer only as a middleman and service provider.<sup>71</sup> The court reasoned that this new licensing model would prevent the merged firm from raising prices because outsourcers would be directly competing for the end users' business.<sup>72</sup> The court therefore found that outsourcing solutions should be included as a competitor in an expanded product market.<sup>73</sup>

More striking is the court's evaluation of Microsoft's potential entry into the up-market HRM field. The court wholly discounted testimony by a Microsoft executive who claimed that the company had no intentions to enter this market.<sup>74</sup> The court explicitly rejected his "humility" about the company's intentions in the field and limited functionality of its product.<sup>75</sup> This conclusion was facilitated after evidence emerged that Microsoft had made a failed attempt to acquire SAP, the third and last player in the government's alleged product market.<sup>76</sup> Adding to the court's distrust was Microsoft's recent alliance with consulting group BearingPoint, which marketed the

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66. *Id.* at 1159.

67. *Id.* at 1158–61.

68. *See id.* at 1101 (finding that the government failed to satisfy the burden of proof entitling it to relief).

69. *Id.* at 1159.

70. *Id.* at 1149.

71. *Id.*

72. *Id.* at 1159.

73. *Id.* at 1149.

74. *Id.* at 1160.

75. *Id.* at 1144.

76. Lohr & Flynn, *supra* note 1.

Microsoft product as high functioning.<sup>77</sup> The court also appeared to give substantial weight to the statement of a BearingPoint representative regarding Microsoft's potential entry into the market: "it's pretty clear they're coming."<sup>78</sup> Finally, the court decided that the barriers to entry that had hindered failed entrant J.D. Edwards in the past—product functionality, services, and reputation<sup>79</sup>—would not pose a problem for Microsoft.<sup>80</sup>

### III.

#### THE ORACLE COURT'S FLAWED ANALYSIS OF POTENTIAL ENTRY

The *Oracle* court stumbled in its analysis of potential entry in three significant ways. First, the court failed to recognize the inherently unreliable nature of potential entry as a factor in antitrust analysis. Second, the court took no steps to ensure the viability of the supposed potential entrants before making them dispositive of the case's outcome, and then exacerbated that failing by assessing the potential entrants during the market definition phase of the trial. Lastly, the court placed a substantially higher burden of proof on the Section 7 plaintiffs than it did on the defendants, reflecting the unfortunate state of the law which requires the government to prove with specificity that potential entrants are not part of the market, while the defendant need only suggest that they could be.

#### A. *Potential Entry Is Too Unreliable a Factor to Warrant Significant Reliance in Antitrust Analysis*

The likely entry of a new competitor and its effect on a market are unpredictable at best and random at worst. Though theories are often advanced claiming to forecast the kinds of actors who will successfully enter a market, there is no formula for predicting with any certainty which players will actually do so. High-technology industries like software development magnify this uncertainty, where innovation is not only constant but can also be jarring to the industry as a whole.<sup>81</sup>

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77. *Id.*

78. *Oracle*, 331 F.Supp.2d at 1135.

79. *Id.* at 1145.

80. *Id.* at 1160.

81. Richard A. Posner, *Antitrust in the New Economy* 1 (John M. Olin Law & Econ., Working Paper No. 106, 2d Series, 2001) (finding that the "new economy" includes the software industry and is marked by high rates of innovation, rapid and frequent entry and exit, and falling average costs).

The *Oracle* court's reliance on Microsoft's potential entry illustrates this problem. Judge Walker states that Microsoft will not have the same entry problems as J.D. Edwards because of its size, reputation, and resources.<sup>82</sup> It is logical to presume, as did Judge Walker, that large established companies are typically more reliable potential entrants. Such companies' extensive resources make possible the innovation necessary to create new products, while their established reputation eases entry into new markets.

Given the importance of innovation in the software industry, however, that assumption cannot be correct. To the contrary, commentators have found that large companies are often poor innovators.<sup>83</sup> Held hostage by their clients and shareholders, these large companies are unable to take the risks necessary to enter uncharted territory.<sup>84</sup> Under this theory, the best potential entrants are not large established firms because they cannot afford the associated risks and lack of customer support for innovation.<sup>85</sup> Instead, the most effective potential entrant may be the smaller upstart firm, willing to take the risks necessary to develop new products and business models, such as those firms that Judge Walker would have discounted in his analysis.

Similarly, large companies are not necessarily adept at responding to market-changing events, implying that they may not be the best candidates for repositioning into a disputed antitrust market.<sup>86</sup> These events could include not only a change in technology, as the literature addresses, but also changes to a market caused by a merger and subsequent SSNIP. Established and successful companies may be the worst at responding to these make-or-break moments because they are reluctant to adapt to the changes they view as threats.<sup>87</sup> By contrast, new young firms can more easily adjust to changes, making them more viable candidates for entry. By blindly accepting that Microsoft could enter simply because of its size and strength, the *Oracle* court ignored these important nuances.

Even if one could accurately predict that entry would take place, it is equally difficult to forecast whether entry will in fact yield the predicted pro-competitive effects alleged. A collection of studies using analytical models shows that potential entry is a poor substitute for

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82. *Oracle*, 331 F.Supp.2d at 1160.

83. See CLAYTON M. CHRISTENSON, THE INNOVATOR'S DILEMMA: WHEN NEW TECHNOLOGIES CAUSE GREAT FIRMS TO FAIL 42-48 (1997).

84. *Id.*

85. *Id.*

86. See ANDREW S. GROVE, ONLY THE PARANOID SURVIVE 19-20 (1999).

87. See *id.*

actual competitors in disciplining markets.<sup>88</sup> These studies demonstrate that although entry—when it occurs—can be an effective pro-competitive force, such success is not guaranteed simply by beginning to compete.<sup>89</sup> Entry itself takes a long time, its effect on the incumbent firms is not apparent at first, and associated risks make survival rates low.<sup>90</sup> Others emphasize that while entry does sometimes counteract competitive problems, those scenarios reflect economic circumstances that rarely exist.<sup>91</sup>

*B. Insufficient Attention Paid to Likelihood of Entry and Its Effects*

The *Oracle* court made potential entry a primary factor in its analysis without engaging the topic in detail or explicitly stating why in this instance such an unpredictable concept should be dispositive. While insisting that the possible entry into competition of outsourcing companies was important to its analysis, the court does not give any details as to why it holds such a belief. In contrast to the Guideline factors that the DOJ must consider when evaluating potential or uncommitted entrants,<sup>92</sup> the *Oracle* court seems to gloss over the issue entirely. The court credits the testimony of an Accenture executive who claims the company will adopt the new one-to-many business model within two years, but does not mention any additional evidence or testimony that would make such a statement credible.<sup>93</sup> Furthermore, assuming that the inclusion of the two-year entry threshold is a nod to the DOJ Guidelines (which it explicitly acknowledges earlier in the opinion),<sup>94</sup> the court has gotten the requirement wrong: for potential entrants to be considered as part of the market under the Guidelines, entry must be anticipated within one year, not two.<sup>95</sup> If the court is using the two-year window allotted for anticompetitive effects analysis (the time within which potential entrants may be considered to alleviate anticompetitive effects of the merger), then the court has failed to analyze the other relevant components of likelihood and sufficiency.<sup>96</sup>

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88. Kwoka, *supra* note 37, at 191–92.

89. *Id.*

90. *Id.*

91. Jonathan B. Baker & Carl Shapiro, *Antitrust Advice for the New Administration: Detecting and Reversing the Decline in Horizontal Merger Enforcement*, 22 ANTITRUST 29, 33 (Summer 2008).

92. See generally GUIDELINES, *supra* note 7, § 3.

93. See *United States v. Oracle Corp.*, 331 F.Supp.2d 1098, 1149 (N.D. Cal. 2004).

94. *Id.* at 1111–12 (discussing the SSNIP analysis laid out by GUIDELINES, *supra* note 7, § 1).

95. See GUIDELINES, *supra* note 7, § 1.321.

96. See *id.* § 3.0.

The DOJ's requirement of timeliness is not an arbitrary imposition. Even if a potential entrant will eventually combat a post-merger price increase, consumers will nonetheless suffer until entry actually occurs.<sup>97</sup> Because antitrust laws are supposed to protect consumers, the DOJ and courts must ensure to as great a degree as possible that entry will in fact occur and deter any price increase.<sup>98</sup> Carl Shapiro, noted economist, professor, and current Deputy Assistant Attorney General for Economics in the DOJ's Antitrust Division, points out that—as a policy matter—the DOJ has determined that entry which is timely, likely and sufficient will limit consumer harm.<sup>99</sup> What little consumer harm still occurs will be offset by merger synergies that are generally overlooked in antitrust analysis.<sup>100</sup> Even if the anticompetitive effects of the merger are likely to be quickly neutralized, Shapiro sees “no principled basis for simply ignoring those *N* months of consumer harm.”<sup>101</sup> The D.C. Circuit agreed in its famous *Microsoft* decision,<sup>102</sup> finding that if no *short-term* substitutes for the merging parties existed that customers would actually use, then the merging parties alone constituted the product market.<sup>103</sup>

Even though the court is not obligated to follow the DOJ Guidelines, it certainly has an interest in upholding the same antitrust laws that the DOJ enforces. By not crediting the agency's analytical framework, the court creates a serious gap in enforcement.<sup>104</sup> At the very least, the court should engage in a more thorough analysis of whether the potential entrant will enter the market quickly enough to limit harm to consumers. This analysis was decidedly lacking in the *Oracle* decision.

Although some argue that the rapid innovation associated with high-technology industries like software require a more relaxed anti-

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97. Carl Shapiro, Professor of Econ., Univ. of Cal. at Berkeley, Testimony Before the Antitrust Modernization Commission 9 (Nov. 8, 2005), <http://faculty.haas.berkeley.edu/SHAPIRO/amcinnovation.pdf>.

98. These goals and rationales are reflected in the text of the DOJ's Merger Guidelines. See generally GUIDELINES, *supra* note 7, §§ 1.3, 3.0.

99. Shapiro, *supra* note 97, at 9.

100. *Id.*

101. *Id.*

102. See generally *United States v. Microsoft*, 235 F.3d 34 (D.C. Cir. 2001).

103. Plaintiff's Trial Brief, *supra* note 47, at 24 (citing *Microsoft*, 235 F.3d at 52–54).

104. See *Roundtable Discussion: Advice for the New Administration*, 22 ANTITRUST 8 (2008) [hereinafter *Roundtable*]; see also J. Gregory Sidak & Hal J. Singer, *Evaluating Market Power with Two-Sided Demand and Preemptive Offers to Dissipate Monopoly Rent: Lessons for High-Technology Industries from the Antitrust Division's Approval of the XM-Sirius Satellite Radio Merger*, 4 J. COMPETITION L. & ECON. 697, 704 (2008).

trust analysis for horizontal merger enforcement,<sup>105</sup> the uncertain nature of entry warrants a more exacting inquiry, not less. A common sentiment in the antitrust world is that existing antitrust law and policy does not adequately address the dynamic nature of innovative industries.<sup>106</sup> To these observers, the software market and other “new economy” industries are marked by high rates of innovation, rapid and frequent entry and exit, and falling average costs, which therefore make the rigidly applied tests of antitrust law and economics inappropriate.<sup>107</sup> The Antitrust Modernization Commission addressed this phenomenon in its report and recommendations to Congress in 2007, recognizing that some industries introduce new products to market every few months, which creates different competitive constraints that may make traditional market power analysis a poor indicator of actual competitive strength.<sup>108</sup>

Oracle agreed. It appeared to argue for limited antitrust review because its industry was “exceptionally dynamic,” featuring not only new competitors but also more sophisticated customers in a rapidly changing environment.<sup>109</sup> Additionally, Oracle found the DOJ’s two-year threshold for entry to be “arbitrary,” stating instead that competition would surely have increased by the time contracts expired in four, six and ten year increments.<sup>110</sup> Although it is unclear whether Judge Walker credited this particular argument, his obvious acceptance of potential entrants without substantial evidentiary proof suggests he may have been more lenient in his evaluation because of the changeable technological market involved. Since *Oracle*, companies under antitrust scrutiny have advanced similar arguments.<sup>111</sup>

Though innovative markets may include a changing cast of characters, antitrust enforcement requires consistent analysis. Rather than reduce or relax antitrust standards for these new economies, existing

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105. Shapiro, *supra* note 97, at 2.

106. *See id.* at 2–3.

107. *See* Posner, *supra* note 81, at 926.

108. *See* ANTITRUST MODERNIZATION COMMISSION, REPORT AND RECOMMENDATIONS at 41 (2007) [hereinafter ANTITRUST MODERNIZATION COMMISSION REPORT].

109. *See* Defendant Oracle Corporation’s Trial Memorandum, *supra* note 47, at 6–7, 25.

110. *See id.* at 25.

111. *See, e.g.,* Sirius/XM, *infra* Part IV.B. Most dramatically, Sirius and XM Radio (the merging parties) proposed the novel concept of “dynamic demand spillover” to avoid the uniformly applied SSNIP test. Sidak & Singer, *supra* note 104, at 702. The parties claimed that existing competition created a free-rider effect that discouraged smaller companies from improving their products and services and engaging in other “demand-enhancing investments.” *Id.* at 731. As discussed below, the DOJ declined to prosecute.

practices are flexible enough to apply to these changing conditions.<sup>112</sup> The Antitrust Modernization Commission agrees, addressing this very question in its most recent congressional recommendation.<sup>113</sup> Rather than propose a change of technique, the Commission found that “antitrust law has sufficient grounding in economic learning and flexibility to provide appropriate analyses of competitive issues in new economy industries.”<sup>114</sup> Much to the chagrin of antitrust defendants, innovative industries do not warrant different rules for antitrust review, but rather continue to be subject to the same standards as everyone else. To grant innovators such a waiver from the law would be “an absurd result.”<sup>115</sup>

The requirement that actors in dynamic industries follow the same antitrust rules as everyone else includes potential entry; the uncertain nature of potential entry necessitates an intensive, fact-specific inquiry for both plaintiffs and defendants, regardless of industry. Some propose extremely stringent standards, suggesting that parties identify a particular product, its location in the development pipeline, and its potential close substitutes in a forecast relevant goods market.<sup>116</sup> Others follow a more general approach, hoping that courts will not rely on “the three ‘E’ arguments”—entry, expansion, and efficiencies—without first finding in the record significant evidentiary support for it.<sup>117</sup> Commentators observe that the pro-competitive effects of potential entry should not rest on only a few possible entrants, since empirical evidence (and the discussion above) shows that not even a single entrant can be predicted with certainty.<sup>118</sup> Following the more moderate approach to potential competition doctrine in *United Tote* and *Franklin Electric*, Shapiro recommends a fact-specific, case-by-case analysis in which participants firmly root their potential entry claims in historical, current, and emerging technological trends, business strategies and capabilities, exit of other parties from the market, and other factors that could impact the competitive landscape.<sup>119</sup> The *Oracle* court’s examination did not meet any of these evidentiary or analytical standards.

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112. See Shapiro, *supra* note 97, at 2.

113. ANTITRUST MODERNIZATION COMMISSION REPORT, *supra* note 108, at 42.

114. *Id.*

115. Shapiro, *supra* note 97, at 3.

116. Ilene Knable Gotts & Richard T. Rapp, *Antitrust Treatment of Mergers Involving Future Goods*, 19 ANTITRUST 100, 102 (2004) (rejecting the alternative approach of evaluating the post-merger combination of R&D capabilities).

117. Baker & Shapiro, *supra* note 91, at 33.

118. Kwoka, *supra* note 37, at 192.

119. Shapiro, *supra* note 97, at 4; see also discussion *supra* Part I.C.

The *Oracle* court exacerbated these failings by applying potential entry to the market definition phase of the trial. It is true that parties may invoke potential entrants as members of a product market<sup>120</sup> or for their impact on a merger's anticompetitive effects.<sup>121</sup> Though in theory *Oracle* and Judge Walker were entitled to use potential entry as a tool in defining the market, their manner of doing so was fundamentally flawed; the court erroneously made market definition the dispositive factor in the litigation while at the same time using an extremely unreliable theory to define it.

As Shapiro notes, finding relevant antitrust markets and market power are "merely intermediate steps."<sup>122</sup> Though necessary, they are only important "to the extent that the resulting market shares are used to infer competitive effects."<sup>123</sup> The important inquiry instead revolves around the competitive consequences of the merger; while litigants must satisfy the transitional steps, the ultimate decision must focus on impact to competition.<sup>124</sup>

Despite the DOJ's showing of anticompetitive effects, the *Oracle* court frontloaded its analysis and formalistically applied the market definition inquiry in a way that made market definition the deal-breaker of the case.<sup>125</sup> Having found that the government had not met its burden to establish the relevant product market, the court would not weigh in on the merger's possible anticompetitive effects. This mistake was error in itself.

When market definition acts as a gatekeeper, as it did in *Oracle*, the factors the court uses to establish the market assume special importance. When courts give undue importance to market definition without reference to anticompetitive effects, as it did in *Oracle*, then those factors become even more powerful. When the court must analyze differentiated products—where no two products are perfect substitutes and a traditional market is difficult to define—the extreme force of market definition is especially clear.<sup>126</sup> One must question

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120. See Bush & Massa, *supra* note 5, at 1043, 1074 n. 287.

121. See *id.* at 1043; Kwoka, *supra* note 37, at 174.

122. Shapiro, *supra* note 97, at 6.

123. *Id.*

124. See Marc G. Schildkraut, *Interpreting Oracle: The Future of Unilateral Effect Analysis*, 19 ANTITRUST MAG. 20, 21 (2005) (observing that "[w]hether or not it is called a market, there is still an anticompetitive effect, isn't there?").

125. See *United States v. Oracle Corp.*, 331 F.Supp.2d 1098, 1101–03 (N.D. Cal. 2004).

126. See Schildkraut, *supra* note 124, at 23. Unlike the altered trial approach that I suggest below, Schildkraut uses the *Oracle* decision to advocate for a modification of the Merger Guidelines. Finding that existing doctrine cannot adequately define a market for differentiated products and that effects analysis adequately describes the com-

whether a court should use so nebulous a theory as potential entry at this stage of analysis at all (though it is technically permissible). At the very least, potential entry should not play such an important role this early in the analysis if it is not accompanied by greater, specific evidentiary support for the proposition. The *Oracle* court required no such proof.

*C. The Court Imposes a Greater Burden on Plaintiffs  
than on Defendants*

The court also erred in the manner in which it imposed burdens of proof on both the government and the defendant. The court required of the defendant almost no evidence in support of its position, while it simultaneously rejected the plaintiff's case for lack of specificity. In so doing, the court essentially denied the government an effective opportunity to disprove its opponent's poorly articulated case.

Although Oracle's assessment of Microsoft as a potential competitor was essentially an affirmative defense to the government's proposed market, the court did not require Oracle to present affirmative proof to support its claim. Defendants do not have to propose their own market definition, and Oracle did not volunteer its own version of the competitive market. Rather, Oracle preferred to dismantle the government's proposal instead.<sup>127</sup>

In relying on potential entry by Microsoft in its decision, however, the court ultimately placed substantial weight on an argument that the defense had not actually made.<sup>128</sup> Oracle's industry witnesses only included executives from "mid-market" competitor Lawson, direct competitor SAP, outsourcer Accenture, and two experts.<sup>129</sup> Notably absent from this list is a representative from Microsoft. One could argue that, given its opportunity to cross-examine a Microsoft witness presented by the government, Oracle was able to sufficiently make its case. But given its centrality to the court's decision, the court should have required Oracle to present independent information concerning this point.

Additionally, Oracle used its witnesses to establish that the proposed product market was overly vague and under-inclusive, but did not go into specifics regarding Microsoft's ability to enter the market

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petitive market, he argues that the DOJ should skip market definition altogether and proceed directly to the analysis of anticompetitive effects. *Id.* at 24.

127. See *Oracle*, 331 F.Supp.2d at 1148.

128. *Id.* at 1160, 1173.

129. *Id.* at 1148-58.

successfully and have a constraining effect on prices.<sup>130</sup> Instead, Oracle appears to have relied on testimony of other industry participants that Microsoft had been aggressively spending in the business software market and otherwise flexing its competitive muscle.<sup>131</sup> Oracle did not even address the issue directly in its trial brief, but rather simply mentions that Microsoft's entry into the enterprise application software market was an example of the industry's "dynamism."<sup>132</sup> Clearly the court did not require very much from Oracle in the way of proof.

Compared to its treatment of Oracle, the court's rejection of the government's witnesses seems particularly unfounded. Whereas the court credited the defense's competitor witnesses regarding Microsoft's role in the industry, it explicitly discarded the customer witnesses that testified on behalf of the plaintiff.<sup>133</sup> The court found that the customer testimony was too self-interested to be credible, and spoke only to present preferences rather than actual future competition.<sup>134</sup> Judge Walker therefore discounted the relevance of their opinions to a possible price increase.<sup>135</sup> Although the defense's witnesses could have been acting in a similarly self-interested manner by inflating their current capacity, the court accepted those particular impressions of future competition regarding Microsoft.<sup>136</sup> Furthermore, the court rejected the government's expert witness because he could not offer a "quantitative metric" by which to measure the relevant market.<sup>137</sup> Although it is unclear whether anything about potential entry could be reliably quantified, the court does not require anywhere near as much specificity from the defense.<sup>138</sup>

Although it is of course possible that the court had a legitimate reason for crediting certain testimony over others, the court did not give any basis for its decision. As a result, it appears that the court arbitrarily held the plaintiff to a much higher standard of proof than it did the defendant. While the court accepted the defendant's potential entry claim without first subjecting the theory to necessary evidentiary safeguards, it required the plaintiff to provide specific evidence to disprove the exact same theory. The process of disproving the existence

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130. *Id.*

131. *See id.* at 1135. *See generally* Lohr & Flynn, *supra* note 1.

132. Defendant Oracle Corporation's Trial Memorandum, *supra* note 47, at 6.

133. *Oracle*, 331 F.Supp.2d at 1131–32.

134. *Id.*

135. *Id.*

136. *Id.* at 1135–36.

137. *Id.* at 1159.

138. This disparity makes the DOJ's decision not to appeal particularly suspect.

of something is difficult enough on its own; to require specific proof on top of that, when the proponent of the fact has done so little to establish its existence, seems unwarranted.

The Guidelines also impose significant restrictions on the DOJ in its efforts to introduce potential entrants as relevant competitors. Although the Guidelines are not mandatory, Division attorneys do look to the Guidelines in conducting their analysis. As a result, one can assume that the government has already engaged in a specific fact-finding mission in order to satisfy the Guidelines' necessary criteria for establishing the existence and relevance of potential entrants by the time it has arrived at trial.

By allowing Oracle to so easily introduce potential entrants, the court has effectively required the DOJ to go into this analysis twice—first in its initial investigation, then again at trial. Moreover, while the court does not ask the defendant to prove that potential entrants *do* exist, it asks the government to show that they do *not*. The court therefore makes the government do all the work by placing little burden of production on the defense and making it too easy for the burden to be shifted back to the plaintiff.

The court facilitated this imbalance by stopping the trial short at the market definition stage. Had the trial proceeded upon the presumption of anticompetitive effects gleaned from a high market share, Oracle would have had the burden of producing evidence to rebut that presumption and show that no anticompetitive impact would result from the merger.<sup>139</sup> The *Oracle* decision therefore demonstrates just how much power the court has in deciding which side must bear the evidentiary burden; the court's simple decision of how to phrase a particular question can change the entire course of the game.

One could argue that this burden shifting arrangement is appropriate because the potential competition doctrine lays out a similar system.<sup>140</sup> Under that doctrine, the government faces a substantial evidentiary burden to establish that a potential competitor's entry is likely to actually take place and be pro-competitive.<sup>141</sup> Defendants, however, are not presumed to have that kind of knowledge available and are therefore not asked to provide it.<sup>142</sup>

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139. *United States v. Baker-Hughes*, 908 F.2d 981, 982 (1990). Of course, Oracle would dispute whether the DOJ would ever be entitled to that presumption at all. See Defendant Oracle Corporation's Trial Memorandum, *supra* note 47, at 25–27.

140. See *Bush & Massa*, *supra* note 5, at 1057–58.

141. See *id.* at 1076.

142. See *id.*

The higher burden employed by the potential competition doctrine, however, is for a very different kind of claim. In those cases, the government is attempting to stop a market participant from acquiring a company that is not yet in the market. In that scenario, it makes sense to limit the government's power because the government is trying to preserve competition that does not yet exist. In that situation, it is appropriate for the court to exact more stringent standards from the government in order to protect defendants from far-reaching claims by the federal government.

*Oracle*, however, did not require such safeguards. The government did not over-reach its mandate, nor was it the proponent of the potential entrants in question. The court may have properly held the defendant Oracle to a lesser standard of proof, but in doing so it then impermissibly placed a much greater burden on the plaintiff. Either the defendant did not advance any independent evidence supporting Microsoft as a potential entrant, or the court simply chose not to address it. Subsequently, the government essentially had to prove the invalidity of potential entry twice—first, as part of its normal horizontal merger analysis under the Guidelines, then at trial under a de facto potential competition doctrine despite the fact that the DOJ was not the proponent of the claim. The posture of the case did not warrant the special protections imposed by the potential competition doctrine's allocation of burdens. Without a rationale requiring it, such a heavy burden is a poor guarantee of justice.

#### IV.

#### ORACLE'S LEGACY: TODAY'S ENFORCEMENT ENVIRONMENT

The *Oracle* decision has had a lasting impact on horizontal merger enforcement. A noticeable decrease in merger challenges by the DOJ since its loss in *Oracle*<sup>143</sup> suggests that the agency has become apprehensive about pursuing enforcement actions to trial, a situation that threatens to prevent the agency from fulfilling its mandate.<sup>144</sup> Moreover, the theory of potential entry has played an im-

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143. Sidak & Singer, *supra* note 104, at 704–06.

144. The Obama Administration recognized a marked decrease in antitrust enforcement action during the Bush Administration when it announced a reinvigorated enforcement policy in May 2009. Stephen Labaton, *Administration Plans to Strengthen Antitrust Rules*, N.Y. TIMES, May 11, 2009, at A1. In so doing, the new Administration reversed the lenient Bush policy limiting enforcement of the anti-monopoly provisions of Section 2 of the Sherman Act. *Id.* This action represents a welcome and necessary first step on the road to renewed antitrust enforcement. However, as this policy shift focuses only on illegal monopolistic conduct, not on Section 7 Clayton

portant but inconsistent role in the Division's own merger analysis, which further threatens the state of antitrust enforcement today.<sup>145</sup>

A. *The Negative Impact on Enforcement: No Action*

The DOJ has not litigated a single merger challenge since *Oracle*. This trend has led many in the field to speculate that the Division's reticence traces to that defeat.<sup>146</sup> Albert Foer, head of the American Antitrust Institute, has stated that "ever since the Oracle-PeopleSoft decision, the common observation has been that the division has been fearful of taking strong positions against mergers."<sup>147</sup> Others attribute the decline to Judge Walker's rejection of the government's customer testimony, surmising that the Division is wary of its ability to effectively stage a merger challenge without such an essential piece of the puzzle.<sup>148</sup> Academics verify this decrease in DOJ

Act merger enforcement, there remains significant work to be done in order to combat the ongoing damage inflicted by the Bush Administration and the *Oracle* decision.

145. Additionally, anecdotal evidence may suggest that Microsoft has not become the powerhouse ERP software provider that the court had predicted, both justifying the government's product market definition and illuminating the court's error. Of course, Microsoft itself insisted at trial that the company would not pursue the large, enterprise level customer base, noting at the time that the company had already delayed development of its new business application suite, "Project Green," by postponing the roll-out from 2004 to 2008. Joris Evers, *Microsoft Puts the Brakes on Next Business Apps*, IDG NEWS SERVICE, June 25, 2004, available at <http://www.info-world.com/article/04/06/24/HNmsbrake>. Even then, Microsoft's development in this area would only approach the upper mid-market and corporate account space in its second release, which was not slated for deployment until 2010 at the earliest. *Id.*

By 2007, delay became cancellation, when Microsoft announced that the integration of its four ERP suites under Project Green would no longer be the company's primary objective. Renee Boucher Ferguson, *Project Green is Dead—for the Foreseeable Future, at Least*, EWEK.COM, Mar. 13, 2007, <http://www.eweek.com/c/a/Enterprise-Applications/Project-Green-is-Dead151for-the-Foreseeable-Future-at-Least>. While maintaining that Microsoft would continue to add functionality to each product so they would resemble each other, the company would no longer focus on a single integrated product. *Id.* The company slated those changes for introduction at some point in the "next decade." Posting of Mary-Jo Foley to ZDNet, Microsoft's Project 'Green': Still alive and kicking, All About Microsoft, <http://www.blogs.zdnet.com/microsoft> (Mar. 13, 2007, 15:20 EST). These delays and cancellations indicate that Microsoft has not made enterprise-level ERP software a priority, highlighting the court's error in making Microsoft the silver bullet in its antitrust analysis.

By contrast, Oracle's strength has appeared to continue undiminished since its acquisition of PeopleSoft. Not only did Oracle announce its \$7.4 billion acquisition of computer hardware producer Sun Microsystems in April 2009, but it has purchased more than forty companies since it bought PeopleSoft five years ago. Ashlee Vance, *Cash in Hand, Technology Giants Go Shopping*, N.Y. TIMES, Apr. 21, 2009, at B1.

146. Sidak & Singer, *supra* note 104, at 704.

147. McClure, *supra* note 3, at 5.

148. *Id.* Former FTC Chairman Timothy Muris finds the *Oracle* court's treatment of customer testimony particularly damaging. *Roundtable*, *supra* note 104, at 19. He

challenges, but also observe that the dips coincide with Republican presidential administrations that favor big business.<sup>149</sup> Regardless of the cause, industry participants believe that there are fewer hurdles to proposed mergers at every level of the review process, including fewer and shorter investigations, weaker acceptable remedies, and virtually no enforcement actions.<sup>150</sup> Perhaps the Division's decision not to appeal the *Oracle* judgment suggests the start of a defeatist attitude that now continues as ongoing silence.

Of course this correlation does not necessarily prove causation, and many argue that there has been no change in DOJ enforcement actions. Former Assistant Attorney General of the Antitrust Division Thomas Barnett, who led the Antitrust Division between 2005 and late 2008, rejects claims of inaction. He suggests that the dearth of trials indicates that the government's efforts to make clear to companies which kinds of mergers will pass regulatory muster have been successful.<sup>151</sup> Barnett and others also remind observers that trials are not the only available method of policing anticompetitive mergers, but rather are supplemented by consent decrees and divestitures.<sup>152</sup> Still, even those who do not find the DOJ's recent silence to be remarkable acknowledge that it "seems pretty clear that the Antitrust Division is much more cautious in challenging mergers than they have been at times in the past."<sup>153</sup>

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remarks that the court's decision reflects "a gulf—a Grand Canyon—between the agencies and the federal courts" on the issue. *Id.* Enforcement agencies and defense lawyers alike rely on customer views as "one of the most important screens" in merger analysis, yet courts appear "hostile" to such arguments. *Id.* When practitioners and judges are not using the same benchmarks, merger enforcement becomes unpredictable, if not impossible. To harmonize the government and courts' views on the subject, Muris wisely suggests analogizing to the Business Judgment Rule from corporate law. *Id.* Following this approach, courts would afford customer testimony the same deference it generally applies to a corporate director's business decisions in the absence of evidence of fraud or self-dealing. This would be a good start in the effort to stabilize the doctrine in this area.

149. Baker & Shapiro, *supra* note 91, at 30.

150. *Id.*

151. McClure, *supra* note 3. A recent example of Division activity may support Barnett's position. In November 2008, Google and Yahoo withdrew from their proposed advertising partnership only hours after the DOJ announced its intention to block the deal. Miguel Helft & Steve Lohr, *Google Won't Pursue Yahoo Ad Deal*, N.Y. TIMES, Nov. 5, 2008, at B1. Perhaps the Division's actions are more credible threats now that such suits are so uncommon. That would suggest to merging companies that they might be better off saving themselves the trouble of litigation. In that light, the DOJ has simply introduced a measure of self-enforcement to the market.

152. McClure, *supra* note 3 at 7; *Roundtable*, *supra* note 104, at 18–19.

153. McClure, *supra* note 3 at 7.

B. *The Negative Impact on Enforcement:  
Inconsistent Entry Analysis*

*Oracle*'s lasting impact seems particularly evident in the Division's treatment of potential entry. In two of the most high-profile mergers in the last several years, the DOJ declined to prosecute based in part on findings that potential entry would limit anticompetitive effects post-merger.<sup>154</sup> These two mergers—of laundry machine manufacturers Whirlpool and Maytag and satellite radio providers Sirius and XM—illustrate how inconsistently even a single agency can apply potential entry to enforcement decisions.

If potential entry is to play a role in horizontal merger analysis, the approach taken in the Division's 2006 clearance of Whirlpool's acquisition of Maytag seems an effective and fair place to start. Despite Whirlpool's post-merger market share of nearly seventy-five percent and head-to-head competition with Maytag in the washing machine market, the DOJ found that the recent entry and potential entry of additional market players indicated that the merger would pose no anticompetitive effects.<sup>155</sup> In particular, the DOJ noted that Samsung and LG had recently entered the U.S. market and could be expected to increase their imports if Whirlpool raised prices after the merger.<sup>156</sup>

In contrast to the *Oracle* decision, the DOJ engaged in a fact-intensive investigation before relying on Samsung and LG as potential entrants capable of maintaining healthy competition in the industry. Rather than simply point to these two companies, as the *Oracle* court did, the DOJ investigated their production and sales efforts in other countries, their relationships with U.S. retailers when first introducing laundry products in recent years, and their current sales success with retailers like Home Depot and Best Buy.<sup>157</sup> As Barnett notes, the DOJ "looked at who [were] the players in the market, was entry possible, if entry had already occurred how quickly it could expand."<sup>158</sup> Also un-

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154. See Press Release, Dep't of Justice, Department of Justice Antitrust Division Statement on the Closing of its Investigation of Whirlpool's Acquisition of Maytag (Mar. 29, 2006), available at [http://www.usdoj.gov/atr/public/press\\_releases/2006/215326.htm](http://www.usdoj.gov/atr/public/press_releases/2006/215326.htm) [hereinafter Whirlpool/Maytag Press Release]; Press Release, Dep't of Justice, Statement of the Department of Justice Antitrust Division on its Decision to Close its Investigation of XM Satellite Radio Holdings Inc.'s Merger with Sirius Satellite Radio Inc. (Mar. 24, 2008), available at [http://www.usdoj.gov/atr/public/press\\_releases/2008/231467.htm](http://www.usdoj.gov/atr/public/press_releases/2008/231467.htm) [hereinafter Sirius/XM Press Release].

155. Roundtable, *supra* note 104, at 17; Whirlpool/Maytag Press Release, *supra* note 154.

156. Whirlpool/Maytag Press Release, *supra* note 154.

157. *Id.*

158. McClure, *supra* note 3, at 3 (quoting Thomas Barnett).

like *Oracle*, this instance of potential entry proved accurate; the imported washers of LG and other companies reach American consumers in advertising and in stores every day.<sup>159</sup>

A less successful analysis of potential entry emerged in the Division's treatment of the Sirius/XM merger. To the casual antitrust observer, the proposed merger of the only two satellite radio providers in existence presented a textbook merger-to-monopoly scenario, ripe for enforcement action.<sup>160</sup> Instead, the DOJ gave its approval after deciding that the proposed merger was not likely to substantially lessen competition.<sup>161</sup> The Division accepted the parties' arguments that alternative services such as AM/FM and HD Radio, MP3 players, and wireless telephone music players were viable competitors to the merging parties. Notably, the Division also agreed that the rapidly changing technological environment would create similar services that would be able to compete with Sirius/XM in the future.<sup>162</sup> Specifically, the Division decided that "next-generation wireless networks" would be able to stream Internet radio to mobile devices: although "it is difficult to predict which of these alternatives will be successful and the precise timing of their availability as an attractive alternative, a significant number of consumers in the future are likely to consider one or more of these platforms as an attractive alternative to satellite radio."<sup>163</sup>

In its decision to approve the merger, the Division relied on potential entry in much the same way as the *Oracle* court; it afforded entrants tremendous weight without first following accepted criteria for establishing their credibility. The Division itself stated that "the likely evolution of technology played an important role in the Division's assessment of competitive effects."<sup>164</sup> The DOJ did not, however, share any specific evidence indicating why it felt the potential entry of mobile broadband Internet devices and other such services was reliable enough to warrant closing its investigation. Nor did it discuss whether the entrants had met the requirements of the DOJ's own Guidelines. To the contrary, the release suggests that the new technologies would fail to meet the specified one- and two-year deadlines imposed by the Guidelines, and instead would only be introduced

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159. See Experience LG, TV Ads 2007, <http://us.lge.com/experience/advertising/tv20075.jsp>; Roundtable, *supra* note 104, at 17.

160. Richard Siklos & Andrew Ross Sorkin, *Merger Would End Satellite Radio's Rivalry*, N.Y. TIMES, Feb. 20, 2007, at A1.

161. Sirius/XM Press Release, *supra* note 154.

162. *Id.*

163. *Id.*

164. *Id.*

“within several years.”<sup>165</sup> Unlike the Whirlpool/Maytag investigation, where the Division described the relevant inquiries made,<sup>166</sup> here the Division offered no information concerning which specific factors made hypothetical future technologies sufficient to combat possible post-merger anticompetitive effects.

The public is not privy to the Division’s internal analysis, so without the disclosure afforded by litigation we cannot know for certain what kinds of evidence the parties presented in support of their potential entry claims. The press release does suggest that the Division appropriately considered potential entrants for their pro-competitive impact rather than merely as members of the market.<sup>167</sup> However, the decision ends up in the same place as *Oracle*, with potential entry playing “an important role” in killing a merger enforcement action.<sup>168</sup> By raising the specter of potential entry itself, the DOJ unwittingly magnified the problems associated with *Oracle*. While *Oracle* amplified the importance of potential entry by moving the unreliable factor from the anticompetitive effects phase to the market definition phase, the DOJ extends the power of potential entry even further by making it a decisive factor even in its initial decision to prosecute.

This aborted investigation represents how dangerously powerful potential entry has become in horizontal merger analysis. Although I argue that the outcome in *Oracle* was wrong, at least in litigation an able judge with an established doctrine should be able to evaluate whether a potential entrant is a sufficiently solid actor to warrant credibility. In Whirlpool/Maytag, potential entrants with specific products already in several markets and a history of U.S. competition were dependable enough to justify termination of the investigation. The Sir-

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165. *Id.* J. Gregory Sidak and Hal J. Singer find in their recent article that the DOJ strayed from its normal operating procedure in several other ways in its decision not to pursue blocking the Sirius/XM deal. Most relevant to our discussion is the continued problem in defining relevant markets. They find that the DOJ improperly accepted the parties’ proffered competitive alternative services because they relied on supply-side information rather than the demand-side information required by the Guidelines. Sidak & Singer, *supra* note 104, at 699. Pointing to the availability of alternatives says nothing about how customers will react to them in the face of a post-merger price increase, thus ignoring the basic tenets of the SSNIP test as reflected in the Guidelines. *See id.* at 709. Sidak and Singer also suggest that the DOJ may have raised its legal standard from the incipency standard used in *Oracle* (“would likely have” anticompetitive effects) to a more exacting likelihood standard (no evidence that the merger “is likely” to have anticompetitive effects). *See id.* at 704–05. Both represent marked departures from the Division’s customary practice.

166. Whirlpool/Maytag Press Release, *supra* note 154.

167. *See* Sirius/XM Press Release, *supra* note 154.

168. *See id.*

ius/XM case did not possess any of these mitigating factors. There was no judge or formal evidentiary proceeding. More importantly, there were no individual companies or products that could be evaluated. Even if the parties and DOJ could point to a type of technology that would eventually compete in this instance, the DOJ's decision to green light the merger ultimately relied on future innovation by unnamed actors who would create undetermined products. This is not how the system should work.

## V.

### PROPOSAL FOR CHANGE: RELIABLE EVIDENCE AND A MORE BALANCED BURDEN

The *Oracle* decision demonstrates the need for a clearer rule concerning potential entry in Section 7 antitrust trials. The law currently scatters differing standards across various procedural scenarios, with no uniform approach in place for parties to follow. The uncertainty stemming from this unsettled area of law is perhaps what led to the flawed reasoning of *Oracle*. Had Judge Walker and the parties been able to look to a firmly established burden-shifting system for the introduction of potential entrants, then perhaps Judge Walker would not have improperly dismissed the action at the market definition phase of the trial. I propose a system that would solve this problem. By requiring the parties to introduce potential entrants through substantial proof as part of a balanced burden-shifting system, judicial supervision of horizontal merger analysis will yield a more equitable outcome.

#### A. *Potential Entry Should Be Evaluated at the Anticompetitive Effects Stage Only*

First, parties and courts should analyze the role of potential entrants at the anticompetitive effects stage of antitrust analysis rather than as part of the effort to define the relevant product market. Potential entry is fraught with uncertainty. By placing this concept at the beginning of a merger analysis, courts only amplify the ambiguity of an already tenuous theory. Furthermore, if potential entrants intrude upon the market definition inquiry, the court too heavily weights that element of a merger challenge, especially where differentiated products are involved. While market definition is merely an intermediary step relevant primarily for its impact on competition, the addition of potential entrants to this stage of analysis gives market definition a gatekeeper function too powerful for the role it is meant to play. The addition of these unpredictable actors gives market definition the abil-

ity to kill a merger challenge before the court can reach the real issue: the potential anticompetitive effects of the merger.

To cure this failing, parties should only consider potential entrants after definitively establishing the product market. As a result, potential entry would become an affirmative defense, allowing the defendant to dispute the alleged anticompetitive effects of the merger. By placing potential entry considerations at this stage of the antitrust analysis, the court would strike a more appropriate balance than it does currently. While the defendant may still invoke potential entry as a mitigating factor, the mere possibility of entry may not itself defeat a merger challenge before the court has addressed the anticompetitive effects of the merger.

*B. Defendant Bears the Burden of Persuasion Regarding Potential Competition as a Defense*

Having established the relevant product market, the defendant may then introduce evidence that potential entrants into that market will alleviate whatever anticompetitive effects the merger may yield. To do so, the defendant must present evidence sufficient to support its position. Unlike in *Oracle*, the court should not require the plaintiff to disprove the existence of an element of the defense before the defendant has presented sufficient evidence to establish its own claim.

This system represents a fair balance of responsibilities. As a general matter, our legal system universally requires proponents of claims to support their own assertions. Just as a tort defendant must provide evidence to support a contributory negligence claim, so must the antitrust defendant prove that its defense is reliable. Similarly, criminal defendants are tasked with proving their own affirmative defenses by sufficient evidence. Neither should antitrust defendants reap the rewards of a defense they have not proven.

Requiring the defendant to bear the burden of persuasion for this particular claim would not diminish the government's already substantial burden in a merger challenge. First, the government retains the ultimate burden of proof in establishing a violation of Section 7. Second, in this new system, the court will not entertain a potential entry theory until after establishing the relevant product market; because the government plaintiff is responsible for proving the product market, the plaintiff will have already satisfied a considerable burden at this point

in the litigation. By comparison, the defendant has done very little.<sup>169</sup> Making potential entry an affirmative defense neither lessens the plaintiff's obligations at trial nor poses an insurmountable obstacle to the defendant. It merely postpones an argument until later in the trial so that the court can ensure a more equitable allocation of responsibilities.

*C. Defendant Must Present Evidence to Support its  
Potential Entry Claim*

Unlike in *Oracle*, the defendant may not merely point to potential entrants as possible competitors, but must instead argue for their reliability based on affirmative evidence. Even at this stage of the analysis, the court should not allow potential entrants to play a significant role without first requiring that the parties substantiate them through appropriate proof. The *Oracle* court tainted its own credibility by demanding quantifiable proof from the plaintiff but only blanket assertions from the defendant. Unlike a criminal trial in which the defense need only plant a seed of doubt in the fact-finder's mind, here the defendant must prove its own case by a preponderance of the evidence. Therefore, the defendant must, at a minimum, advance at least some evidence on its own behalf.

Although the courts of appeals (or Supreme Court) would be free to adopt different permutations in establishing this system, I propose that courts consider the DOJ Guidelines when looking for an appropriate standard of proof by which to establish potential entry. The Guidelines require that potential entry be timely, likely, and sufficient before the Division may consider its effect on post-merger competition. This standard is flexible enough to account for the uncertain nature of potential entry. However, it is also sufficiently specific to assure the court that the potential entrants will in fact do what the defense suggests. The court must be concerned with the consumer harm that takes place between the consummation of the merger and the entrant's start of business.<sup>170</sup> As a result, the defendant must be able to show that the potential entrant will enter the market in a timely fashion so as not to prolong consumer harm, and that the new business will be successful enough to be profitable and competitive.

It bears mention that entry need not be proven to a certainty to survive judicial scrutiny. As then-Judge Thomas wrote, such certainty

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169. Remember, the defendant has no obligation to propose its own definition of a relevant product market and instead may simply pick apart the government's definition, as did *Oracle*.

170. Shapiro, *supra* note 97.

would be nearly impossible to achieve.<sup>171</sup> Instead, courts should look to the fact-based inquiries undertaken in potential competition doctrine. Although *Marine Bancorp.* asked too much, requiring a showing that the potential entrant would have a significant pro-competitive effect on the market, other courts' standards under the same doctrine appear more attainable.<sup>172</sup> Requiring "reasonable probability" that a potential entrant will actually enter successfully balances the need for evidence with the acknowledgement that clear proof may be difficult to obtain.

#### D. Possible Criticism

Critics may find fault with this proposed system. The foremost criticism could be that potential entry is too unpredictable a theory and is therefore an inappropriate topic for proof requirements generally, and unfair to the defendant specifically. This argument fails to appreciate the fundamental uncertainty that underlies all merger analysis in antitrust law. Section 7 of the Clayton Act deals entirely with future possibilities, assessing the *probability* that consumer harm will result from a proposed merger based on hypothetical questions of what the parties *could* do once merged.<sup>173</sup> Good or bad, the law is engaged in this kind of inquiry already, so to dismiss consideration of the potential entrant as too uncertain would be to ignore the nature of the antitrust system already in place.

A more specific objection would be the difficulty the defense would encounter in obtaining the necessary proof to assert a potential entry defense. As then-Judge Thomas pointed out in *Baker-Hughes*, potential competitors are unlikely to hand over information regarding their internal business plans to the companies against whom they hope to someday compete.<sup>174</sup> The proposal put forth here, however, does not require specific internal planning documents. All it asks is enough to show the reasonable probability that entry could occur successfully.

There are many ways in which the defendant could satisfy this relatively low standard. For example, the more lenient version of potential competition doctrine for defendants suggests a number of factors that courts have considered persuasive in evaluating the viability of potential entrants.<sup>175</sup> The defense could introduce evidence regarding the industry as a whole, showing that there are enough incentives

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171. Bush & Massa, *supra* note 5, at 1076.

172. *See id.* at 1057, 1128.

173. *See* 15 U.S.C. § 18 (2006).

174. Bush & Massa, *supra* note 5, at 1076.

175. *See id.* at 1078.

to enter the market that entry is in fact likely to take place. Similarly, the defendant could share past entrant success stories, perhaps including information on the entrant's ability to constrain market prices, timelines for entry, and customer responses to the new product offerings. If entry has not yet occurred, the defendant could present evidence related to the effect on the defendant's prices of having the potential competitor on the fringe of the market. That the merger takes place in a rapidly changing innovative market is no excuse, since the Antitrust Modernization Commission has already insisted that new economy industries do not deserve special treatment under the anti-trust laws.<sup>176</sup> Having made this preliminary showing, the burden shifts back to the plaintiff government to prove that entry is not reliable. The government's civil investigative demand<sup>177</sup> power makes it better able to obtain specific business information from the entrants itself, if necessary.

Others could argue that there is some value in having a higher burden on the government than on defendants in general, and that this proposal's reallocation is therefore inappropriate and unjustified. As in criminal trials, it is ultimately fair to make the government work harder so that the system can provide better procedural protections for the defendant. However, those critics should consider the types of defendants involved in these antitrust trials and whether major corporations engaged in multi-billion dollar mergers really need such added legal protection against the government. The government does not have the unbridled power that some might assume. In fact, limited government resources and the sheer wealth that large corporations have at their disposal would indicate much to the contrary.

Regardless, this proposal has not fundamentally realigned the burdens involved, but has rather shifted them to reflect a more equitable balance. Moreover, the posture of a case in which the defendant invokes potential entry as a defense does not warrant the special protections afforded under potential competition doctrine, where the government uses potential entry as the basis for its merger challenge. While the defendant corporation may deserve the extra protection when the government uses potential entry as a sword, it does not follow that the same is necessary when the defendant uses potential entry as a shield.

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176. ANTITRUST MODERNIZATION COMMISSION REPORT, *supra* note 108, at 42.

177. The civil investigative demand (CID) is similar to a subpoena.

## CONCLUSION

The *Oracle* court's blind acceptance of potential entry showcases the lamentable state of the law in this area. If we continue in this manner, enforcement of the antitrust laws will suffer. The law must allow the DOJ to do its job. If that is to happen, defendants must take responsibility for their own claims, and courts must engage the important issues head-on before dismissing cases on potential entry grounds.

Potential entry can be used by different actors in different ways and under different evidentiary standards. This jumble of doctrine inevitably leads to regrettably uninformed decision-making. While courts should consider potential entry as a legitimate factor in merger analysis, they should not accept so uncertain a theory after only a cursory glance. Instead, courts must insist that they will only consider potential entry under specific circumstances during the trial, and only when supported by sufficient proof. In this way, courts will avoid the flawed analysis displayed in *Oracle*, and will use relevant and reliable information to make more reasonable decisions.

