Recent Merger Challenges Show DOJ and FTC Focus on Nascent Competition

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Introduction

Concern about protecting "nascent" competition is a hot topic in the antitrust world. In particular, enforcement authorities and others are expressing heightened interest in acquisitions of small emerging competitors or potential competitors that could represent a serious future threat to dominant incumbent firms. Recent merger challenges by both the Department of Justice, Antitrust Division ("DOJ") and Federal Trade Commission ("FTC"), as well as other enforcement authorities outside the United States, have brought issues relating to elimination of nascent competition to the forefront.

These enforcement actions are consistent with recent agency priorities, and demonstrate the agencies' willingness to challenge mergers—almost always a predictive enterprise even in conventional cases—on increasingly aggressive grounds. We anticipate that this focus will continue and intensify at the agencies as new Biden appointees take office. In addition, as discussed below, we expect similar trends in other jurisdictions and we note the possibility of legislative action in this area.

As a result, firms contemplating transactions should be mindful when undertaking acquisitions of smaller, arguably innovative firms, even if such firms are not currently direct or obvious competitors. Similarly, smaller firms should be cognizant of the enhanced risks of a sale to a larger industry incumbent.

Background on Nascent Competition

To understand current concerns regarding nascent competition, it is helpful to view the concept against the backdrop of the more established "potential competition" doctrine, through which the U.S. antitrust agencies address acquisitions between parties that do not currently compete but where the agencies predict one party will in the future enter one of the other party's markets.

Nascent competition can include potential competition, but is a broader concept. Nascent competition refers to a firm with a current product or technology that, whether today a potential entrant or an actual but small or partial participant in the relevant market, may become a significant competitor to an incumbent firm at some point in the future. Nascent competition thus includes not just rivals waiting on the periphery, but also rivals that are already in the relevant market but might currently have negligible shares. Whereas potential competition looks at the prospect for future entry, nascent competition looks in addition at the prospects for future growth once such entry has occurred.

The U.S. antitrust agencies have increasingly applied the concept to scrutinize and challenge acquisitions where the target is a current producer (or developer of a pipeline product) that may become a meaningful rival, as well as acquisitions of firms whose preparation or threat to enter the relevant market causes incumbent firms to keep prices low to head off potential entry. Accordingly, recent enforcement actions feature distinct kinds of targets: some with products in development, some with existing products or production capability that do not compete today, and some with products that do compete today but only to a minor or incomplete degree.

While agencies and courts have not yet developed a clear distinction between "potential" and "nascent" competition, what is clear is that antitrust authorities are increasingly concerned about the potential elimination of competitive threats to strong companies in either established or emerging markets,

particularly in technology and R&D-focused industries. The authorities (much less the courts) have not yet, however, coalesced around a clean articulation of the doctrine of nascent competition or how it should be applied in different types of enforcement actions. Courts have imposed fairly demanding requirements on enforcers seeking to prove that an acquisition target is a potential competitor. How agencies and courts will treat the similarly predictive enterprise of assessing the significance of nascent competition is still a work in progress, although several recent actions are instructive.

Recent agency actions targeting nascent competitive concerns: Visa/Plaid and P&G/Billie

Both the DOJ and FTC have recently filed complaints to block proposed acquisitions based on concerns about nascent competition.

In November 2020, the DOJ sued to block Visa's proposed acquisition of Plaid, alleging that the acquisition would eliminate a nascent competitive threat to Visa's alleged monopoly in online debit services.[1] The complaint acknowledges that while Plaid's existing technology does not compete directly with Visa today, Plaid was planning to leverage its technology, combined with its existing relationships with banks and consumers, to facilitate transactions between consumers and merchants in competition with Visa.[2] The complaint further alleges that Visa viewed Plaid as an emerging competitor and decided to acquire Plaid to protect against a "threat to [Visa's] important US debit business."[3] Notably, the DOJ alleged that the proposed acquisition violates both Section 2 of the Sherman Act (monopolization) and Section 7 of the Clayton Act (acquisition that may reduce competition). Visa announced in January 2021 that it was abandoning the deal.

Similarly, in December 2020, the FTC announced that it would file an administrative complaint to block Procter & Gamble's ("P&G") proposed acquisition of Billie, Inc., alleging that the acquisition would eliminate competition in women's wet razors. The FTC alleges that P&G is a monopolist in both men's and women's razors, and that Billie is a new and expanding maker of women's razors.[4] As Ian Conner, the Director of the FTC's Bureau of Competition, put it: "Billie was likely to expand into brick-and-mortar stores, posing a serious threat to P&G. If P&G can snuff out Billie's rapid competitive growth, consumers will likely face higher prices."[5] P&G announced in January 2021 that it was abandoning the deal.

Visa/Plaid and P&G/Billie Suggest a Trend

These recent agency actions are not isolated cases, but rather reflect an increased focus by the antitrust enforcement agencies and policy makers on nascent competition. There are a few points to note here:

First, nascent competition has been the subject of increasing agency and academic focus. For example, the FTC held a hearing addressing acquisitions of potential or nascent competitors in October 2018 as part of its Hearing on Competition and Consumer Protection in the 21st Century. As recently as November 2020, Joe Simons, Chairman of the FTC, discussed the framework for assessing acquisitions of nascent competitors, stating that enforcers must be "willing and able to recognize that harm to competition might

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[1] Justice Department Sues to Block Visa's Proposed Acquisition of Plaid, Dept. of Justice (Nov. 5, 2020), **https://www.justice.gov/opa/pr/justice-department-sues-block-visas-proposed-acquisition-plaid**.

[2] Complaint, *United States v. Visa Inc. and Plaid Inc.*, 3:20-cv-07810, at ¶ 8 (N.D. Cal. Nov. 5, 2020), **https://www.justice.gov/opa/press-release/file/1334726/download**.

[3] *Id*.

[4] FTC Sues to Block Procter & Gamble's Acquisition of Billie, Inc. (Dec. 8, 2020), **https://www.ftc.gov/news-events/press-releases/2020/12/ftc-sues-block-procter-gambles-acquisition-billie-inc?utm_source=govdelivery**.

[5] *Id*.

not be obvious from looking at the marketplace as it stands."[6] Makan Delrahim, the Assistant Attorney General for Antitrust at the DOJ, has echoed similar concerns, acknowledging that acquisitions of nascent competitors can sometimes be anticompetitive and that such "circumstances may raise the Antitrust Division's suspicions."[7]

Second, the agencies have undertaken a number of other investigations and challenges to mergers, in addition to Visa/Plaid and P&G/Billie, over the last few years, based on alleged harm to nascent competition.[8] Some of these cases include:

- **Roche's Acquisition of Spark Therapeutics (2019)**: The FTC conducted an extensive investigation into the acquisition to determine whether the proposed transaction would eliminate a nascent competitive threat to Roche's existing treatment for Hemophilia A. The FTC concluded that the evidence did not support a conclusion that the transaction would be likely to reduce competition and harm consumers.[9]
- **Illumina Acquisition of Pacific Bio (2019)**: The day after closing its Roche/Spark investigation, the FTC challenged Illumina's acquisition of Pacific Bio, asserting that the acquisition "would eliminate a nascent competitive threat" to Illumina's monopoly power in DNA sequencing.[10] The complaint also alleged that the proposed acquisition was illegal because it may substantially lessen competition in the U.S. market for next-generation DNA sequencing by eliminating current competition and preventing future competition between the parties.[11] The parties abandoned the deal in early 2020.
- **Edgewell's Proposed Acquisition of Harry's (2020)**: In a similar case to the P&G/Billie deal (discussed above), the FTC sued to block the proposed merger of Edgewell, which owns the number two men's razor brand, Schick, and Harry's, a much smaller shaving company. The FTC alleged that Harry's was a "critical disruptive rival that has driven down prices and spurred innovation in an industry that was previously dominated by two main suppliers," Edgewell (Schick) and P&G (Gillette).[12] The parties ultimately abandoned the deal.
- **Investigation into Facebook's Acquisitions of Instagram and WhatsApp (2020)**: After a long retrospective investigation, the FTC filed a complaint against Facebook alleging that its

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[6] Prepared Remarks of Chairman Joseph J. Simons at the ABA Section of Antitrust Law Fall Forum 2020 (Nov. 12, 2020), **https://www.ftc.gov/system/files/documents/public_statements/1583022/simons_-_remarks_at_antitrust_law_fall_forum_2020.pdf**.

[7] Assistant Attorney General Makan Delrahim Delivers Remarks for the Antitrust New Frontiers Conference (June 11, 2019), **https://www.justice.gov/opa/speech/assistant-attorney-general-makan-delrahim-delivers-remarks-antitrust-new-frontiers**.

[8] Note, Davis Polk represented clients in Roche/Spark and the Facebook investigation.

[9] Statement of the Fed. Trade Comm'n, *In the Matter of Roche Holding/Spark Therapeutics*, Comm'n File No. 1910086 (F.T.C. Dec. 16, 2019), **https://www.ftc.gov/system/files/documents/public_statements/1558049/1910086_roche-spark_commission_statement_12-16-19.pdf**.

[10] Complaint, *In the Matter of Illumina, Inc. and Pacific Biosciences of Cal., Inc.*, Comm'n File No. 1910035, at ¶ 81 (F.T.C. Dec. 17, 2019), **https://www.ftc.gov/system/files/documents/cases/d9387_illumina_pacbio_administrative_part_3_complaint_public.pdf**.

[11] *Id*. at ¶¶ 84–86.

[12] FTC Files Suit to Block Edgewell Personal Care Company's Acquisition of Harry's, Inc. (Feb. 3, 2020), **https://www.ftc.gov/news-events/press-releases/2020/02/ftc-files-suit-block-edgewell-personal-care-companys-acquisition**.

acquisitions of Instagram (in 2012) and WhatsApp (in 2014) illegally maintained its monopoly in "personal social networking" by eliminating nascent competitors to its core Facebook product.[13]

Third, there has been some indication of potential legislative change to address this issue. The House Subcommittee on Antitrust, Commercial and Administrative Law recommended in October 2020 that Congress evaluate potential legislation to protect nascent competition, including potentially "codifying a presumption against acquisitions of startups by dominant firms."[14]

Fourth, focus on nascent competition is not limited to the United States. The U.K. Competition and Markets Authority ("CMA") is increasingly seeking to review cases that potentially threaten nascent competition, particularly in the digital and pharmaceutical sectors, conducting in-depth investigations into Roche/Spark and Illumina/Pacific Bio, despite the very limited UK nexus of the two deals. Andrea Coscelli, the CMA's Chief Executive, has also previously recognized that elimination of a "nascent competitor could remove an important source of competition" and argued for reviews to assess the long-term future growth potential of merging companies in addition to expected near-term market developments.[15]

The European Commission is also currently taking steps to allow for closer scrutiny of transactions that raise nascent competition issues. From mid-2021, the Commission will accept referrals from EU Member States to conduct reviews of transactions, even where national-level jurisdictional thresholds are not satisfied. This policy shift is said to be driven by a desire to investigate deals in sectors where there may have been historic under-enforcement and, in particular, to allow for detailed investigations of proposed acquisitions of nascent competitors by technology companies.[16]

Takeaways

- The agencies are likely to undertake investigations and possibly challenge acquisitions—across industries—where they see potential harm to nascent competition.
- The nascent competition doctrine is not necessarily confined to merger challenges. As noted above, the DOJ's challenge to Visa/Plaid and the FTC's recent complaint against Facebook allege violations of the monopolization provision of the Sherman Act. It is also possible that if courts broaden the concept of "competitor" to include nascent competitors, this could impact conduct cases under Section 1 of the Sherman Act or Section 5 of the FTC Act (i.e., a larger group of "competitors" that could potentially enter into an anticompetitive conspiracy).
- Firms that have a sizeable market share and that are contemplating purchasing a small, emerging competitor or "innovator"—even one with no current overlapping sales and no fully overlapping product or R&D project—should closely analyze whether recent enforcement actions indicate potential antitrust issues. This analysis is complicated by that fact that the target may presently sit outside of the direct marketplace in which the acquiring firm participates.

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[13] FTC Sues Facebook for Illegal Monopolization (Dec. 9, 2020), **https://www.ftc.gov/news-events/press-releases/2020/12/ftc-sues-facebook-illegal-monopolization**.

[14] Investigation of Competition in Digital Markets, House Subcommittee on Antitrust, Commercial and Administrative Law (Oct. 4, 2020), **https://judiciary.house.gov/uploadedfiles/competition_in_digital_markets.pdf**.

[15] Andrea Coscelli, Speech on Competition in the digital age: reflecting on digital merger investigations (June 3, 2019), **https://www.gov.uk/government/speeches/competition-in-the-digital-age-reflecting-on-digital-merger-investigations**.

[16] Margrethe Vestager, Speech on the future of EU merger control (Sept. 11, 2020), **https://ec.europa.eu/commission/commissioners/2019-2024/vestager/announcements/future-eu-merger-control_en**.

- Similarly, smaller firms may want to take these considerations into account when considering a potential sale.
- Companies (whether large or small) should also be mindful of how to handle the antitrust risk that theories of harm regarding nascent competition can present, including when negotiating risk allocation and termination provisions in merger agreements.
- Finally, while nascent competition issues often arise in life sciences/pharmaceutical and high tech industries, these issues are not limited to these sectors. For example, the P&G/Billie and Edgewell/Harry's deals both involved the decidedly analog businesses of men's and women's razors.

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