
Unit 5B: H&R Block/TaxACT

Part 2. Anticompetitive Effect and Defenses

Professor Dale Collins
Merger Antitrust Law
Georgetown University Law Center



TaxAct®

Typical structure of a formal merger analysis

■ Step 1: The prima facie case

A. Relevant market

- *Brown Shoe* “outer boundaries” and “practical indicia” tests for product markets
- “Commercial realities” test for geographic market
- Hypothetical monopolist test [and other 2023 Guidelines tests to the extent adopted]

B. *PNB* presumption

- Market participants and market shares
- Application of the *PNB* presumption ← { Judicial precedent
Guidelines thresholds [to the extent adopted]

C. Other evidence of anticompetitive effect

- Unilateral effects
- Coordinated effects
- Elimination of a maverick

H&R Block

■ Step 2: Defendants’ rebuttal

A. Challenges to the prima facie case (failure of proof on upward pricing pressure)¹ ←

B. Traditional defenses

- Entry/expansion/repositioning
- Efficiencies
- Countervailing buyer power (“power buyers”)
- Failing company/division

■ Step 3: Court resolves factual issues and determines net effect on competition

Defendants' rebuttal arguments

■ Four arguments

1. The likelihood of expansion by existing DDIY firms besides Intuit, HRB, and TaxACT will offset any anticompetitive effects
2. The relevant market is not susceptible to coordination and the merger will not increase the probability of effective coordinated interaction
3. The merger will not result in anticompetitive unilateral effects
4. The efficiencies resulting from the merger will offset any anticompetitive effects

Explicit Theories of Anticompetitive Harm: Coordinated Effects

Introduction

■ Definition

- Coordinated effects (or coordinated interaction) is a theory of anticompetitive harm that depends on the merger making oligopolistic interdependence more effective:

Merger law “rests upon the theory that, where rivals are few, firms will be able to coordinate their behavior, either by overt collusion or implicit understanding in order to restrict output and achieve profits above competitive levels.”¹

Think price fixing without an agreement

- **Terminology:** May use “accommodate” rather than “coordinate” or “cooperate”
- **Scope:** Firms can coordinate across any or all dimensions of competition, including price, product features, customers, geography of operation, innovation, wages, or benefits²

¹ FTC v. CCC Holdings Inc., 605 F. Supp. 2d 26, 60 (D.D.C. 2009); *accord* United States v. H&R Block, Inc., 833 F. Supp. 2d 36, 77 (D.D.C. 2011).

² See 2023 Merger Guidelines § 2.3.

Introduction

■ Relation to Sherman Act § 1

- Section 1 provides explicit coordination by agreement on competitive variables that can be manipulated to harm consumers and increase producer profits
- Section 7 addresses tacit coordination, that is, coordination that occurs in the absence of agreement (and hence cannot violate Section 1)

Rule: Since Section 7 prohibits mergers with a reasonable probability of lessening competition, a merger is anticompetitive if it increases the likelihood, effectiveness, or stability of coordinated interaction.

A Section 7 violation does not require proof that firms in the market would engage in such coordination as a result of the merger.

Introduction

- What can firms do if the merged firm seeks to increase price?
 1. *Do nothing*: Just continue doing what they were doing
 2. *Compete more aggressively*: Expand production/maybe even lower price to gain market share from the firms that are increasing their prices
 3. *“Accommodate” the price increase*: “Pull their competitive punches”
 - Need not match the price increase
- Key question:

Will the merger increase the probability of effective coordinated interaction/ accommodating conduct among some or all the firms in the market, thereby facilitating the exercise of market power to the harm of consumers?
- Key requirement:
 - Must find a causal relationship between the merger and the increased probability, effectiveness, or stability of tacit coordination

Merger Guidelines history

1. 1982 Guidelines

- ❑ Accepted an unspecified theory of oligopoly as the underpinning of the *PNB* presumption
- ❑ Did not require more for a prima facie case

Merger Guidelines history

2. 1992 Guidelines

- ❑ *Problem:* There exist highly competitive markets with only a few firms
 - E.g., Coke and Pepsi
- ❑ *Solution:* Require proof that the “Stigler conditions” for (tacit) coordination were satisfied in the relevant market:
 - Stigler conditions {
 1. *Tacit agreement:* Market conditions must be conducive to firms (tacitly) reaching terms of coordination that are individually profitable to the firms involved
 2. *Detection:* Market conditions must be conducive to firms detecting deviations from the tacit terms of coordination
 3. *Punishment:* Market conditions must be conducive to firms punishing deviations from the tacit terms of coordination
- ❑ *In practice:*
 - The courts—and, indeed, many within the agencies—did not understand the punishment requirement
 - Many thought that it required participating firms to tacitly reach an agreement on a particular punishment and then tacitly coordinate to implement it
 - Prosecutors had a difficult time convincing courts to accept proof that market conditions were conducive to punishing deviations and the theory grew out of favor

Merger Guidelines history

3. 2010 Merger Guidelines

- The 2010 Merger Guidelines sought to revitalize the coordinated effects theory
- *Solution*: Eliminate the language of the Stigler conditions and focus more generally and less prescriptively on—
 - 1. The premerger *susceptibility* of coordinated interaction, and
 - 2. The *effectiveness* of the merger in increasing the likelihood, effectiveness, or stability of coordinated interaction among some or all the firms in the market
 - Requires a causal relationship between the merger and the increased probability of effectiveness of coordination
- Relation to the Stigler conditions
 - The 2010 susceptibility requirement subsumed the structural market, information, and incentive compatibility considerations inherent in the first two Stigler conditions
 - The Stigler punishment element disappeared altogether as a factor in the analysis and was replaced by the effectiveness condition
 - Effectiveness only requires a showing of an increased likelihood of successful coordinated interaction, not proof that coordination interaction would in fact occur postmerger

2010 MG requirements

Merger Guidelines history

3. 2010 Merger Guidelines (cont.)

- Adoption of the 2010 Merger Guidelines test by the courts has been mixed
 - Some courts have adopted the 2010 Merger Guidelines two-element test¹
 - Other courts continue to use the *H&R Block* approach of:
 - Presuming coordinating effects when postmerger concentration is sufficiently high to trigger the *PNB* presumption, *and*
 - Shifting the burden (presumably of production) to the merging parties to rebut the presumption²
 - If the burden is one of persuasion, the shift violates *Baker Hughes*

¹ See *New York v. Deutsche Telekom AG*, 439 F. Supp. 3d 179, 234 (S.D.N.Y. 2020); *FTC v. RAG-Stiftung*, 436 F. Supp. 3d 278, 317 (D.D.C. 2020).

² See *United States v. Bertelsmann SE & Co. KGaA*, 646 F. Supp. 3d 1, 44-45 (D.D.C. 2022) (“[W]hen the government has shown that a merger will substantially increase concentration in an already concentrated market, . . . ‘the burden is on the defendants to produce evidence of “structural market barriers to collusion” specific to this industry that would defeat the “ordinary presumption of collusion” that attaches to a merger in a highly concentrated market.’”) (quoting *H&R Block*, 833 F. Supp. 2d at 77); *FTC v. OSF Healthcare Sys.*, 852 F. Supp. 2d 1069, 1087 (N.D. Ill. 2012).

Merger Guidelines history

4. The 2023 Guidelines refinements

- a. *Consistent terminology*: While the 2010 Merger Guidelines use "coordinated interaction," "coordinated conduct," and "coordinated effects" interchangeably, the 2023 Merger Guidelines uses the term "coordinated interaction" consistently
- b. *Extension to nonprice dimensions*: Adopted the approach of the 2010 Guidelines but explicitly recognized that coordinated interaction can occur across multiple dimensions of competition in addition to price, including product features, customer segmentation, output, innovation, and (on the input side) labor market conditions such as wages and benefits¹
 - *WDC*: Expect the major focus in cases to be on price unless the evidence in a particular case is materially probative of likely coordination on other dimensions
 - In this connection, a history of past attempts of coordination on a specific dimension is likely to be regarded by the agencies as highly probative
- c. *Simplify the proof*
 - The 2023 Guidelines collapse the two-element 2010 test into one requirement: does the merger increase the "likelihood, stability, or effectiveness of coordination" in the relevant market?
 - Simplifies the proof by listing three "primary factors" presumptive and five "secondary factors" probative in showing the coordinated effects theory applies to a merger

¹ 2023 Merger Guidelines § 2.3.

Evidence bearing on coordination

- 2023 Merger Guidelines
 - Identify three primary factors and five secondary factors

Primary Factors

A highly concentrated market after a significant increase in concentration

Prior actual or attempted coordination in the relevant market

Elimination of a maverick or other disruptive competitor

Evidence bearing on coordination

- 2023 Merger Guidelines
 - Identify three primary factors and five secondary factors

Primary Factors	Secondary factors
A highly concentrated market after a significant increase in concentration	Market concentration
Prior actual or attempted coordination in the relevant market	Visibility of competitive variables in the market
Elimination of a maverick or other disruptive competitor	Predictability and speed of competitive responses
	Aligned incentives
	Profitability or other advantages of coordination

The primary factors support an agency inference of susceptibility and increased risk; the secondary factors can establish increased risk even without a primary factor.

The modern approach

- The 2023 Guidelines ask one ultimate question:

Does the merger increase the “the likelihood, stability, or effectiveness of coordination” in the relevant market?

- For analysis, it helps to retain the 2010 framework’s two components:
 1. Premerger susceptibility

Are market conditions conducive to firms reaching and sustaining accommodating conduct?

2. Merger effectiveness

Will this merger materially increase the likelihood, stability, or effectiveness of coordination?

For a Section 7 violation, the plaintiff must still connect the merger to an increased coordination risk; market susceptibility alone is not enough

Premerger susceptibility

- Three coordination problems

1. Selection

Can firms identify a mutually profitable focal point?

Relevant evidence: Signals, simple terms, product similarity, aligned incentives

Premerger susceptibility

■ Three coordination problems

1. Selection

Can firms identify a mutually profitable focal point?

Relevant evidence: Signals, simple terms, product similarity, aligned incentives

2. Internal stability

Will each participant prefer accommodation to defection?

Relevant evidence: Observability, frequency of interaction, gains from cheating, detection

Premerger susceptibility

■ Three coordination problems

- | | |
|--------------------------|--|
| 1. Selection | Can firms identify a mutually profitable focal point?

Relevant evidence: Signals, simple terms, product similarity, aligned incentives |
| 2. Internal stability | Will each participant prefer accommodation to defection?

Relevant evidence: Observability, frequency of interaction, gains from cheating, detection |
| 3. External interference | Can outsiders disrupt or defeat the coordinated outcome?

Relevant evidence: Entry, expansion, fringe capacity, powerful buyers, substitution |

Coordinated effects in *H&R Block*

■ Coordinated effects in *H&R Block*

□ Court:

Since the government has established its prima facie case, the burden is on the defendants to produce evidence of “structural market barriers to collusion” specific to this industry that would defeat the “ordinary presumption of collusion” that attaches to a merger in a highly concentrated market.¹

- This is consistent with a strict reading of *Baker Hughes* only if the plaintiffs have established a prima facie case of coordinated effects
 - BUT *H&R Block* in effect rebuttably presumes a prima facie case of coordinated effects when the PNB presumption is triggered
 - Courts taking the *H&R Block* approach typically cite to *Heinz*, a D.C. Circuit case decided in 2001²
 - This illustrates that precedent can trump the Merger Guidelines
 - The *H&R Block* approach is contrary to the approach of the 2010 Horizontal Merger Guidelines
- Other courts follow the 2010 Merger Guidelines and require the plaintiff to prove a prima facie case of coordinated effects through a showing that—
 - The relevant market is susceptible to coordinated effects, *and*
 - The merger will increase the likelihood or effectiveness of coordinated effects

¹ United States v. H & R Block, Inc., 833 F. Supp. 2d 36, 77 (D.D.C. 2011) (quoting FTC v. H.J. Heinz Co., 246 F.3d 708, 725 (D.C. Cir. 2001)).

² *Id.*

Coordinated effects in *H&R Block*

- Merging parties' arguments
 1. Intuit has no incentive to compete any less vigorously postmerger
 2. In particular, Intuit has no incentive to reduce competitiveness of its free product, since free products are a principal driver of paid new customers to Intuit
 3. Therefore, HRB must compete vigorously postmerger or else lose customers to Intuit

Coordinated effects in *H&R Block*

- Evidence: Premerger susceptibility
 1. Three firms could form the “collusive group”
 - Fringe firms too insignificant to be able to disrupt coordination among the “Big Three”
 2. Historical coordination
 - After TaxACT introduced its free offering, Intuit proposed that firms lobby the IRS to impose limits on their free offerings (HRB and others joined, but not TaxACT)
 - *Court*: “Highly persuasive historical act of cooperation”
 - *WDC*: Shows that evidence does not have to be of historical illegal coordination
 3. Other factors
 - Market is transparent (consumer offerings—prices and features available on the Internet)
 - Product differentiation not that relevant
 - Companies can observe and coordinate on attributes of “free” products
 - Transactions are small, numerous, and spread among a mass of consumers
 - Consumers have low bargaining power
 - Significant barriers to switching due to “stickiness” of DDIY products (learning curve)

Coordinated effects in *H&R Block*

- Evidence: Increase in postmerger effectiveness
 1. *Contra*: Intuit engaged in “war games” designed to anticipate and defuse new competitive threats that might emerge from HRB postmerger
 2. BUT the merger reduces the “collusive group” from 3 to 2
 3. AND Intuit’s documents also indicated that it anticipated that the combined firm would likely “pull some of its punches” if Intuit is willing to go along and not compete aggressively against it
 - Anticipates that combined firm will “not escalate fee war”
 - *WDC*: This could have been just a random observation by an Intuit employee and not Intuit’s considered strategy
 4. AND past cooperation as to lobbying the IRS for eligibility restrictions for free tax products probative of postmerger cooperation to further restrict eligibility
 5. AND merger would result in the elimination of a “particularly aggressive competitor” (TaxACT) in a highly concentrated market

Coordinated effects in *H&R Block*

■ Court

- Acknowledges that Intuit and the merged company will have strong incentives to compete for customers
- BUT coordination does not have to be on all dimensions of competition
 - One aspect is enough
 - For example, lower the quality of “free” products, causing marginal customers to switch to paid software → making them worse off
 - Here, DOJ alleges “coordination would likely take the form of mutual recognition that neither firm has an interest in an overall ‘race to free’ in which high-quality tax preparation software is provided for free or very low prices.” (p. 77)
 - That is, not eliminate free products (useful as marketing devices)
 - Rather, reduce their quality to drive more customers into paid products
- Conclusion:
 - Defendants failed to rebut presumption that anticompetitive coordinated effects would result from the merger
 - To the contrary, the preponderance of the evidence indicated that coordinated effects likely would result

The practice today

■ Last choice as a theory

- Today, even after the 2010 revisions to the Merger Guidelines, the agencies are hesitant to lead a merger challenge with a coordinated effects theory
 - *Exception:* Where the merger eliminates a “maverick”
- Given the narrow market definitions usually found under the hypothetical monopolist test:
 - In problematic mergers, the merging firms tend to have high market shares and be close competitors with one another
 - Typically yields an easily understood unilateral effects theory
- *Result:* Coordinated effects is rarely used in investigations or litigations as the primary theory of anticompetitive harm
 - Usually more of an add-on theory in the complaint
 - Or when the agency is forced into it (*CCC/Mitchell*)

A final note

- A largely unrecognized asymmetry—The “price ratchet”
 - It is relatively hard for firms to tacitly coordinate to *increase* prices
 - *Problem:* Some firm has to lead the price increase, and if other firms do not follow, the putative price leader will suffer a profit loss → A risky gamble for the putative price leader
 - Some exceptions
 - An established price leader already exists
 - Where price increases can be announced in advance and retracted if insufficient firms follow
 - It is much easier for firms to tacitly coordinate *not to decrease* prices
 - Say there is a common cost increase to suppliers in the market (e.g., fuel prices increase)
 - All firms increase their prices to cover this increased cost
 - Then there is a common cost decrease (e.g., fuel prices decrease)
 - WHAT DO THE FIRMS DO?
 - If one decreases price, other firms will decrease their prices → Market shares stay the same, but profits decline given the price decrease
 - So the usual strategy is for each firm to maintain price and wait for another firm to trigger a price decrease
 - But if all firms follow this strategy, market prices will not decrease in the wake of a common cost decrease

WDC: The antitrust risk of coordinated interaction comes primarily from firms tacitly coordinating to maintain prices when common costs decrease rather than coordinating to increase prices from prevailing levels