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Is the Customer Never Right? *Bazaarvoice* and Customer Testimony in Merger Litigation

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BASED ON EXTENSIVE STATISTICS, Hughston M. McBain, the president of the Marshall Field & Co. department store, concluded that the customer "is sometimes wrong—but he is right often enough to justify the generalization that he is *always* right."[1] This generalization traditionally applied to merger enforcement.

In *United States v. Bazaarvoice, Inc.*,[2] however, the government's case did not largely depend on customer testimony. In contrast to many prior merger cases, and despite the merger having been consummated, the government did not present customer witnesses regarding the competitive effects of the merger. The defendant, on the other hand, chose the traditional customer-centric strategy, emphasizing that none of the 104 customers who testified complained about the merger.[3] According to the defendant, the government's failure to present customer complaints "seriously undermine[d] any claim that customers will be harmed by the merger."[4] The court nonetheless ruled for the government, finding that "it would be a mistake to rely on customer testimony about effects of the merger."[5]

Bazaarvoice thus provides additional fuel for the ongoing debate about the utility of customer testimony in merger litigation. A superficial reading of the court's opinion might lead one to believe that customer testimony no longer has any place in proving (or disproving) potential competitive effects. But a closer read reveals a more nuanced treatment of customer testimony. Coupled with other recent case law, *Bazaarvoice* holds a number of lessons for antitrust litigators presenting customer testimony at trial.

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The Agencies' Evolving Merger Trial Strategy

The Federal Trade Commission and Department of Justice have long stressed the importance of customer testimony in merger enforcement. In 2002, one FTC official described customer views as "very important in merger investigations," "not only to understanding the relevant market" but "also to understanding the potential effects of the mergers."[6] In 2004, the DOJ Assistant Attorney General remarked that customers are "the most objective marketplace participants," their incentives are generally aligned with protecting competition, and "the decisions they make in the ordinary course of business frequently provide a better window onto how the market actually functions than an economist's model or the court's intuition."[7] In their 2006 joint Commentary on the Horizontal Merger Guidelines, the agencies stated that "customers typically are the best source, and in some cases they may be the only source, of critical information on the factors that govern their ability and willingness to substitute in the event of a price increase."[8] And the 2010 Horizontal Merger Guidelines maintain that information "from customers about how they would likely respond to a price increase . . . may be highly relevant," and that the "conclusions of well-informed and sophisticated customers on the likely impact of the merger itself can also help the Agencies investigate competitive effects."[9]

More recently, however, the government seems to have changed its tune, at least with regard to customer testimony in merger litigation. In presenting its winning 2011 case in *United States v. H&R Block, Inc.*,[10] the DOJ eschewed customer testimony. As the then-Acting Assistant Attorney General explained:

> The real lesson of *H&R Block* for the private bar is how we told our story. In past merger trials, the division has sought to present its case in large part through customer witnesses. That approach provided mixed results and we needed a new strategy. In *H&R Block*, we decided to make our case primarily through the parties' own documents and testimony from their executives.[11]

In *Bazaarvoice*, the government went further. Not only did the DOJ forgo presenting substantial customer testimony, but it also called Bazaarvoice's reliance on the testimony of over 100 customers "a sideshow that is intended to distract the court's attention from the real issue in this case."[12] The government seemed to saying that, at least when it comes to predicting the competitive effects of a merger, the customer is *never* right.

The *Bazaarvoice* Trial

The *Bazaarvoice* trial brought into sharp focus the use of customer testimony in merger litigation. The case involved a post-consummation challenge to the acquisition by Bazaarvoice, which the court described as "the unquestioned market leading provider of Ratings and Reviews platforms ('R & R') to companies involved in online commerce," of its "primary competitor," PowerReviews.[13] The government contended that the relevant market was limited to R&R platforms sup-

plied to U.S. customers, that the merger significantly increased concentration in that market, and that the merger would likely result in significant unilateral effects.[14] Bazaarvoice contested the government's market definition and market share data, but the thrust of its attack was the contention that the government failed to prove likely harm to competition. According to Bazaarvoice, the government failed to show harm to the market as a whole (rather than to some individual customers) and potential entry and expansion precluded competitive harm.[15]

The parties' trial strategies were starkly different. The government focused on the parties' pre-merger internal documents, arguing that they unambiguously showed "Bazaarvoice's intent to reduce competition through the acquisition of PowerReviews" and demonstrated "(1) the significance of the pre-merger competition between Bazaarvoice and PowerReviews; (2) the gap separating PowerReviews from other competitive alternatives; and (3) the barriers to entry that insulate Bazaarvoice from future competition."[16] Bazaarvoice, in contrast, highlighted the testimony from over 100 customers, contending they "reflect the diversity of demand in the market," were "sophisticated businesspeople who assessed their options and made a variety of different . . . choices," and only had in common "well-informed views that they were unharmed."[17]

A close examination of the *Bazaarvoice* opinion and recent case law reveals that customer testimony is alive and well in merger litigation, even on the issue of potential competitive effects.

These strategies led to substantial argument regarding how the court should view the customer testimony. The government argued that the customers simply were not competent to assess the competitive effects because they "just aren't trained . . . nor do they have the necessary information" to compare the actual world with the but-for world without the merger.[18] Bazaarvoice, on the other hand, pointed out that the "the government's own official commentary" focused on the perspective of "informed customers," and insisted that the customers were "the ones with the incentive to investigate alternatives, negotiate the best pricing, and select a best solution," and emphasized that "[u]nlike the economic experts, their jobs depend on doing this well."[19] According to Bazaarvoice, customer testimony should be taken seriously because if "the acquisition was likely to harm them in any way, they're the ones with the motive to complain"[20] and customer views "are normally dispositive."[21]

The court sided with the government. After "listening to the testimony of 40 witnesses, reading more than 100 depositions, reviewing 980 exhibits, and considering" the parties' arguments,[22] the court found the customer testimony lacking:

> [C]ustomers generally do not engage in a specific analysis of the effects of a merger. Many of them had given no thought to the effect of the merger or had no opinion. They lacked the same information about the merger presented in court, including from the economic experts. Their testimony on the impact and likely effect of the merger was speculative at best and is entitled to virtually no weight.[23]

Is Customer Testimony Dead After *Bazaarvoice*?

It is tempting to say that *Bazaarvoice* shows that customer testimony now has a limited role in merger litigation. After all, the government relied heavily on customer testimony in back-to-back losses in 2004. In *United States v. Oracle Corp.*,[24] Judge Vaughn Walker dismissed the testimony of "extremely sophisticated buyers" with "decades of experience in negotiating in [the] field," finding their testimony to be "largely unhelpful," mere "speculation," and nothing more than "unsubstantiated customer apprehensions."[25] A week later, in *FTC v. Arch Coal, Inc.*,[26] Judge John Bates found the customer testimony to offer "little more than a truism of economics: a decrease in the number of suppliers may lead to a decrease in the level of competition."[27] Both judges later published articles explaining their views of customer testimony.[28] Perhaps the government learned its lesson, and *Bazaarvoice* puts the nail in the coffin for customer testimony.

Another view is that *Bazaarvoice* confirms the distinction between customer testimony about past conduct and customer testimony about future decisions and effects.[29] According to Judge Bates, for instance, customer testimony regarding historical facts "can be relevant to a number of topics in a merger case, including as an explanation for certain pricing or market behavior, . . . as context for determining how the market truly operates, and as evidence relating to market definition and substitutability."[30] On the other hand, he dismissed "forward-looking" customer testimony that requires "predictions or projections about the future."[31]

But both of these views are too simplistic. A close examination of the *Bazaarvoice* opinion and recent case law reveals that customer testimony is alive and well in merger litigation, even on the issue of potential competitive effects. The key lesson for antitrust litigators is to focus on the quality of and the purpose for which customer testimony is presented.

A Roadmap for Customer Testimony at Trial

The *Bazaarvoice* court relied on customer testimony (including forward-looking testimony) in a number of critical areas. The case thus gives litigators a roadmap for the use of customer testimony at trial.

Proving the Relevant Product Market. Central to proving the relevant market in merger litigation is the hypothetical monopolist test, which asks whether consumers would turn to substitutes in response to a hypothetical monopolist imposing "a small but significant and non-transitory increase in price" (SSNIP) on a particular set of products.[32] The test

thus seeks to predict how customers would react to a hypothetical price increase.

Reliance on customer testimony regarding this issue has been questioned. In *Oracle*, the government presented a number of witnesses who testified they would not switch to alternative products in the face of a price increase. But Judge Walker found this testimony wanting because it "was not backed up by serious analysis that [the customers] had themselves performed."[33] He explained that the government customer witnesses "each testified, with a kind of rote, that they would have no choice but to accept a ten percent price increase by [the merged entity]. But none gave testimony about the cost of alternatives to the hypothetical price increase . . . ."[34] The court also stated that "plaintiffs' customer witnesses did not, in their testimony, provide the court with data from actual or probable . . . purchases and installations" that would demonstrate they had "no choice but to submit" to a price increase.[35] Judge Walker later wrote: "Unsubstantiated conjecture regarding a customer's predicted reaction to a post-merger price increase reflects nothing more than customer 'preferences' developed in the pre-merger environment."[36]

In light of the fact that most customers will not have conducted a course-of-business analysis bearing on potential product market price increases, what can litigators do to enhance the value of customer testimony on the issue of the relevant product market?

Use customer testimony in a supporting role. Although there was no indication the customers performed any "serious analysis" backing their testimony, the *Bazaarvoice* court specifically relied on customer testimony to undergird its findings on the relevant market. Adopting the government's proposed product market definition, the court found that "many customers testified that they would not abandon R&R platforms (or even their R&R platform provider) in the face of a price increase."[37] The court thus found, "based on customer testimony, a SSNIP of five to ten percent would not be unprofitable because few customers would abandon R&R in response to such a SSNIP."[38]

Instead of being front and center in the government's case, this customer testimony was only one of several factors supporting the government's expert's opinion. The court found the testimony was "consistent" with the expert's conclusions.[39] Other supporting evidence included the merging companies' pre-merger return-on-investment analysis, the companies' deal documents, and pre-merger price competition between the companies.[40] The government had presented the customer testimony in a supporting role.

Carefully frame your questions based on the relevant economic test. Economic tests for product market definition are very specific; they seek to discover how customers would react to a small but significant non-transitory price increase. Counsel thus need to be cognizant of the "garbage-in, garbage-out" principle: Asking the wrong question can result in worthless answers.

In *H&R Block*, H&R Block, which produced a popular digital-do-it-yourself (DDIY) tax return preparation product, sought to acquire the maker TaxACT, another popular DDIY product. The defendants contended that DDIY products compete with the old-fashioned "pen-and-paper" method. To support this contention, the defendants commissioned a customer survey that "asked one primary question: 'If you had become dissatisfied with TaxACT's price, functionality, or quality, which of these [listed] products or services would you have considered using to prepare your federal taxes?'"[41] The defendant's expert used the survey results to estimate "diversion ratios," concluding that a substantial percentage of customers would switch to pen-and-paper if dissatisfied with TaxACT.[42]

In response, the government pointed out "that the phrasing of the survey question—which asks about dissatisfaction with 'TaxACT's price, functionality, or quality'—appears to ask a hypothetical question about *switching*, not diversion based solely on a price change."[43] According to the government, the survey question conflated "customer concerns about price, functionality, or quality" such that it could not "shed any light on customer reactions to price changes alone."[44] The court agreed with the government and refused to rely on the customer responses in the survey. The lesson: Frame your questions carefully.

Elicit testimony that explains the reasons for the customer's response. Customer testimony regarding the likely response to a price increase is most persuasive when the customer explains the bases for the testimony. In *Bazaarvoice*, the testimony from customers regarding whether they would switch in the face of a price increase was bolstered by evidence regarding the commercial importance of the products. The court noted that "[w]itness after witness testified to the effect that R&R is considered 'critical' to the business of many online retailers . . . as consumers now expect ratings and reviews to be a part of their online shopping experience."[45]

Similarly, in *FTC v. Lundbeck, Inc.*,[46] the court relied on customer testimony regarding the factors influencing purchasing decisions. In that case, the government contended that two drugs used to treat a life-threatening heart condition in infants competed in the same market. Despite the fact that the drugs were used to treat the same condition, the district court found that the drugs were not in the same market because they had a very low cross-elasticity of demand.[47] The district court found that "neonatologists decide which drug a patient receives" and relied on neonatologist testimony that the "relative price of the drugs does not factor into the choice of drug treatment."[48] The neonatologists explained "that treatment decisions are based solely on perceived clinical advantages/disadvantages" of the drugs.[49] Satisfied with this explanation, the court based its product market findings almost solely on the customer testimony, and the Eighth Circuit affirmed.

Proving Potential Competitive Effects. Customer testimony about potential competitive effects is perhaps the

most controversial. On the one hand, especially in unilateral effects cases, it seems intuitively correct that customers who live, work, and die in the market would have special insight into the potential effects of a merger. Courts, in fact, have chided the government when it has not presented customer testimony complaining of potential adverse effects.[50] On the other hand, the judges in *Oracle* and *Arch Coal* were dismissive of such testimony. As Judge Bates wrote,

> The predictive power of economics far outreaches the similar power of any individual in the industry, no matter how intelligent or experienced that individual may be. Working at Oracle does not make one an oracle, and unless the executive moonlights as a professor or can travel through time, she will not be able to testify directly as to the future events that are at the center of the court's inquiry.[51]

But an assertion that customer testimony has no role in assessing potential competitive effects is too broad. As *Bazaarvoice* and recent merger cases show, customer testimony is still essential to proving the likelihood of competitive effects. Careful litigators can use customer testimony to bolster their competitive effects case.

Elicit testimony about the viability of other providers. One of the key defense arguments in *Bazaarvoice* was that competitive effects were unlikely because other providers could expand sufficiently to defeat any price increase. In rejecting this contention, the court relied on customer testimony when evaluating the viability of these alternatives. For instance, based on customer testimony, the court found that one alleged alternative was "hindered by its lack of reputation in the United States."[52] It also relied on customer testimony to find that another alleged alternative was not viewed as sufficiently robust or as having strong enough capabilities.[53] The court especially noted the reasons why customers had abandoned an alleged alternative.[54] The court also relied heavily on customer testimony in determining whether customers switching to in-house alternatives would constrain prices post-merger.[55]

Focus on customers' requirements that create barriers to entry. The parties in *Bazaarvoice* also sparred over whether sufficient barriers would prevent timely entry that would preclude competitive effects. Relying on customer testimony, the court found that reputation was one barrier to entry.[56] Other recent merger decisions also relied on customer testimony regarding barriers to entry. In *Chicago Bridge & Iron Co. v. FTC*,[57] the court relied on customer testimony that reputation was an important factor in choosing a supplier.[58] And in *FTC v. CCC Holdings Inc.*,[59] the court found that "experience and scale are legitimate barriers to entry" in the relevant markets.[60]

Ensure that any opinions regarding potential effects are based on solid experience and foundation. Although it extensively relied on customer testimony in its evaluation of likely effects, the *Bazaarvoice* court refused to rely on customer opinions regarding whether the merger would cause competitive harm. In doing so, the court catalogued a number of reasons that provide useful guidance for antitrust litigators.

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The customers did not intensely study the R&R market. The court explained: "Products such as R&R platforms are relatively inexpensive in comparison to a company's operating budget and have relatively long contracts. Considering competitive alternatives for R&R is not part of customers' day-to-day activities and most do not have much current information about the prospective effect of a merger."[61] For instance, the court quoted one customer stating, "[i]f I'm not in the market to buy ratings and review services at the moment, I'm not up to speed on that current service, managing hundreds of different vendors. I look at them when they're needed, not continually research everything that's out there all the time."[62]

Many customers had little basis for their opinions. Some customer witnesses admitted "they had never given any thought to the merger."[63] Others were "unaware of alternatives or had conducted a limited review of their alternatives."[64] Some gave an opinion on the effects of the merger even though they "did not currently use a commercial R&R platform."[65]

Customers also had limited visibility into the market. The court found that "[p]rice is negotiated individually with each customer, based on the customer's need and Bazaarvoice's ability to customize its product and sell additional features to the customer."[66] Because of this, the customers could not testify about pricing in the market as a whole.

Based on these and other concerns, the court found the customer "testimony on the impact and likely effect of the merger was speculative at best and is entitled to virtually no weight."[67]

The lessons for antitrust litigators are obvious. The utility of customer opinion testimony on potential competitive effects will vary from market to market and customer to customer. In some markets, customers will spend time and money studying and understanding the market, suppliers, and even the potential effects of the merger. In others, the merger simply is not important to the customers. In some markets, customers can testify about the market as a whole, in others they have only a narrow view. The decision on whether to make customer opinions regarding the effects of a merger central to your trial strategy has to take into account these factors.

Conclusion

Is the customer always right? Not in merger litigation. Is the customer never right? After *Oracle* and *Arch Coal*, many thought that was the case. At first glance, *Bazaarvoice* seems to support that conclusion. But in reality, *Bazaarvoice* shows that customer testimony continues to play a vital role in merger litigation and provides a host of lessons for antitrust litigators. ■

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[1] Hughston M. McBain, *Are Customers Always Right?*, ROTARIAN, Nov. 1944, at 32, 33, *available at* books.google.co.uk/books?id=qUIEAAAAMBAJ&lpg=PP1&pg=PA32#v=onepage&q&f=false.

[2] United States v. Bazaarvoice, Inc., No. 13-cv-00133, 2014 WL 203966 (N.D. Cal. Jan. 8, 2014).

[3] Id. at *4.

[4] Defendant's Post-Trial Brief at 16, United States v. Bazaarvoice, Inc., No. 13-cv-00133 (N.D. Cal. Oct. 25, 2013) [hereinafter Defendant's Post-Trial Brief].

[5] *Bazaarvoice*, 2014 WL 203966, at *4.

[6] David Scheffman, Dir., Bureau of Econ., Fed. Trade Comm'n, Sources of Information and Evidence in Merger Investigations, Address at Mergers and Acquisitions: Getting Your Deal Through in the New Antitrust Climate 3 (June 14, 2002), *available at* www.ftc.gov/sites/default/files/documents/public_statements/sources-information-and-evidence-merger-investigations/scheffmanabanycbar.pdf.

[7] Thomas O. Barnett, Deputy Assistant Att'y Gen., Antitrust Div., U.S. Dep't of Justice, Antitrust Enforcement Priorities: A Year in Review, Remarks Before the Fall Forum of the Section of Antitrust Law 14 (Nov. 19, 2004), *available at* www.justice.gov/atr/public/speeches/206455.pdf; *see also* Deborah Platt Majoras, Chairman, Fed. Trade Comm'n, Antitrust Practice—How Does It Affect European Business? Remarks Before the Studienvereinigung Kartellrecht 10 (Apr. 7, 2005), *available at* http://www.ftc.gov/sites/default/files/documents/public_statements/u.s.antitrust-practice-how-does-it-affect-european-business/050411brussels.pdf ("Customers are valuable sources of information about many mergers' competitive effects because they have the most to lose from an anticompetitive deal . . . .").

[8] U.S. Dep't of Justice & Fed. Trade Comm'n, Commentary on the Horizontal Merger Guidelines 9 (2006), *available at* http://www.justice.gov/atr/public/guidelines/215247.pdf.

[9] U.S. Dep't of Justice & Fed. Trade Comm'n, Horizontal Merger Guidelines § 2.2.2 (2010) [hereinafter Horizontal Merger Guidelines], *available at* http://www.justice.gov/atr/public/guidelines/hmg-2010.pdf.

[10] 833 F. Supp. 2d 36 (D.D.C. 2011).

[11] Joseph F. Wayland, Acting Assistant Att'y Gen., Antitrust Div., U.S. Dep't of Justice, Litigation in the Antitrust Division, Remarks as Prepared for the Georgetown Law 6th Annual Global Antitrust Enforcement Symposium 12 (Sept. 19, 2012), *available at* www.justice.gov/atr/public/speeches/287117.pdf.

[12] Plaintiff's Trial Brief and Motion in Limine at 42, United States v. Bazaarvoice, Inc., No. 13-cv-00133 (N.D. Cal. Aug. 26, 2013).

[13] *Bazaarvoice*, 2014 WL 203966, at *1.

[14] Plaintiff's Post-Trial Brief at 5–17, United States v. Bazaarvoice, Inc., No. 13-cv-00133 (N.D. Cal. Oct. 29, 2013) [hereinafter DOJ Post-Trial Brief].

[15] Defendant's Post-Trial Brief, *supra* note 4, at 10–23.

[16] DOJ Post-Trial Brief, *supra* note 14, at 1.

[17] Defendant's Post-Trial Brief, *supra* note 4, at 15.

[18] Transcript of Proceedings at 2131–32, United States v. Bazaarvoice, Inc., No. 13-cv-00133 (N.D. Cal. Oct. 15, 2013).

[19] *Id.* at 2143.

[20] *Id.*

[21] *Id.* at 2179.

[22] *Bazaarvoice*, 2014 WL 203966, at *2.

[23] *Id.* at *61.

[24] 331 F. Supp. 2d 1098 (N.D. Cal. 2004).

[25] *Id.* at 1130–31.

[26] 329 F. Supp. 2d 109 (D.D.C. 2004).

[27] *Id.* at 146.

[28] *See* Vaughn R. Walker, *Search for a Competition Metric: The Role of Testimony of Customers, Competitors and Economists*, 2 COMPETITION L. INT'L 3 (2006); John D. Bates, *Customer Testimony of Anticompetitive Effects in Merger Litigation*, 2005 COLUM. BUS. L. REV. 279 (2005).

[29] *See, e.g.*, Ken Heyer, *Predicting the Competitive Effects of Mergers by Listening to Customers*, 74 ANTITRUST L.J. 87, 90 (2007) (distinguishing between customer testimony about the "traditional building blocks of merger analysis" and testimony about the customer's preference for whether the "merger should be blocked.").

[30] Bates, *supra* note 28, at 285.

[31] *Id.* at 286.

[32] Horizontal Merger Guidelines, *supra* note 9, § 4.1.1.

[33] *Oracle*, 331 F. Supp. 2d at 1131.

[34] *Id.*

[35] *Id.*

[36] Walker, *supra* note 28, at 3.

[37] *Bazaarvoice*, 2014 WL 203966, at *29.

[38] *Id.* at *67.

[39] *Id.* at *29.

[40] *Id.* at *29–30.

[41] *H&R Block*, 833 F. Supp. 2d at 69.

[42] *Id.*

[43] *Id.* at 70.

[44] *Id.*

[45] *Bazaarvoice*, 2014 WL 203966, at *22.

[46] 650 F.3d 1236 (8th Cir. 2011).

[47] *Id.* at 1240.

[48] *Id.*

[49] *Id.*

[50] *See, e.g.*, FTC v. Butterworth Health Corp., 946 F. Supp. 1285, 1299 (W.D. Mich. 1996) (noting that the government had turned up "remarkably little" opposition to the merger); New York v. Kraft Gen. Foods, Inc., 926 F. Supp. 321, 351 (S.D.N.Y. 1995) ("Plaintiff offered no evidence that retailers object to, or have been harmed by, the Acquisition.").

[51] Bates, *supra* note 28, at 287.

[52] *Bazaarvoice*, 2014 WL 203966, at *41.

[53] *See id.* at *41–42.

[54] *Id.* at *41, *43.

[55] *See id.* at *43–45.

[56] *Id.* at *53.

[57] 534 F.3d 410 (5th Cir. 2008).

[58] *Id.* at 438.

[59] 605 F. Supp. 2d 26 (D.D.C. 2009).

[60] *Id.* at 55.

[61] *Bazaarvoice*, 2014 WL 203966, at *61.

[62] *Id.* (internal quotation marks omitted).

[63] *Id.*

[64] *Id.* at *62.

[65] *Id.*

[66] *Bazaarvoice*, 2014 WL 203966, at *4.

[67] *Id.* at *61.