HIT THE RESET BUTTON: VIDEO GAMES, PLATFORMS, AND CHANGING ANTITRUST VERTICAL MERGER POLICY

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ABSTRACT

For decades, antitrust law has treated vertical mergers as almost per se legal. Courts and scholars embraced the economic theories of the Chicago School, which predict that vertical mergers almost always lead to efficiencies that benefit consumers through lower prices. As a result, vertical mergers are almost never challenged and those that are usually fail. More recently, politicians, regulators, and pundits have become increasingly concerned with the growing concentration of wealth and power among America's large technology corporations. Part of their dominance can be explained by the rapid rise of platform business models, which through network effects can entrench dominant incumbents. Some view antitrust laws as a possible remedy, and stronger vertical merger enforcement among its solutions.

An unlikely culprit—video games—became center stage when the Federal Trade Commission challenged Microsoft's $68.7 billion acquisition of Call of Duty maker, Activision Blizzard. The merger, if approved by global antitrust regulators, would be the largest ever in the video game industry and would create one of the world's largest gaming companies. A once fringe leisure activity, video games have become the largest entertainment industry in the world. The industry is undergoing rapid consolidation with console makers—largely Microsoft and Sony—buying up game studios. With a dearth of case law on vertical mergers, the Microsoft-Activision challenge became one of the first where antitrust agencies attempted to hit the reset button on vertical merger policy. Further, as the most studied industry on platform competition, video games provide an excellent way to explore how these types of firms face different incentives post-merger.

This Article explores vertical merger policy in the context of platforms and uses the Microsoft-Activision merger as a case study for future platform vertical merger enforcement. It argues that dominant digital platforms face unique profit incentives that when combined with a vertical merger may make anticompetitive outcomes more likely.

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I. INTRODUCTION

"To put it simply, companies that once were scrappy, underdog startups that challenged the status quo have become the kinds of monopolies we last saw in the era of oil barons and railroad tycoons."

–House Subcommittee on Antitrust, Commercial, and Administrative Law[1]

In an era of extreme partisanship, politicians have managed to find a common enemy—Big Tech. Though they may disagree on solutions, politicians on both sides of the aisle think America's largest technology companies have accumulated too much power.[2] The House Subcommittee on Antitrust, Commercial, and Administrative Law opened an investigation into Big Tech in 2019, and in July 2020, the Subcommittee hailed the CEOs of Alphabet, Amazon, Apple, and Facebook into Congress to defend their companies' records on competition.[3] Two years later, the Subcommittee published its findings and recommendations in a 364-page document that outlined its grievances with Big Tech.[4]

Summarizing its investigation, the Subcommittee noted three major competitive concerns: "First, each platform now serves as a gatekeeper over a key channel of distribution."[5] The Subcommittee explained that their market control allows Big Tech to "pick winners and losers throughout our economy" and abuse that power "by charging exorbitant fees, imposing oppressive contract terms, and extracting valuable data from the people and businesses that rely on them."[6] Second,

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1 STAFF OF SUBCOMM. ON ANTITRUST, COM., & ADMIN. L., 117TH CONG., INVESTIGATION OF COMPETITION IN DIGITAL MARKETS 2 (2d Sess. 2022) [hereinafter *House Antitrust Report*], https://www.govinfo.gov/content/pkg/CPRT-117HPRT47832/pdf/CPRT-117HPRT47832.pdf [https://perma.cc/E299-YM3L].

2 *See generally* Kiran Stacey & Dave Lee, *Big Tech Rattled as US Antitrust Push Finds Rare Bipartisan Backing*, FINANCIAL TIMES (Jan. 23, 2022), https://www.ft.com/content/d6cb3541-beef-4335-a0d0-ce5d6585e53d [https://perma.cc/ME4W-MZYK] (discussing bipartisan backing of the American Innovation and Choice Online Act).

3 Celine Kang & David McCabe, *Lawmakers, United in Their Ire, Lash Out at Big Tech's Leaders*, N.Y. TIMES (Jul. 31, 2020), https://www.nytimes.com/2020/07/29/technology/big-tech-hearing-apple-amazon-facebook-google.html [https://perma.cc/Q3BE-TZGJ].

4 *See generally House Antitrust Report*, *supra* note 1, at 1–2 (summarizing findings).

5 *Id.* at 1.

6 *Id.*

the Subcommittee found that as gatekeepers, Big Tech firms use that power to maintain their dominant positions.[7] In exercising this power, "they have surveilled other businesses to identify potential rivals, and have ultimately bought out, copied, or cut off their competitive threats."[8] Third, Big Tech firms have "abused their role as intermediaries to further entrench and expand their dominance" and do so through "self-preferencing, predatory pricing, or exclusionary conduct."[9]

As these findings suggest, one such way these firms entrench their market power is through mergers. Alphabet, Amazon, Apple, and Facebook have alone acquired more than 500 companies since 1998.[10] The pushback on Big Tech has coincided with a large rise in market concentration, with fewer firms controlling most of the market.[11] Yet, most of these acquisitions have gone unchallenged by federal antitrust regulators and none have been blocked.[12] Empirical evidence suggests that the Federal Trade Commission's ("FTC") and the Department of Justice's ("DOJ" and collectively "the Agencies") inactivity has resulted in a great deal of underenforcement with the Agencies acting in only 38% of mergers that resulted in price increases for consumers.[13]

Even rarer, vertical merger challenges have been nonexistent. Until the DOJ's suit to block AT&T's acquisition of Time Warner in 2017, neither agency had challenged a vertical merger since the 1970s.[14] Around that time, Robert Bork and other Chicago School scholars had started to convince the antitrust world that vertical mergers create efficiencies that benefit consumers through lower prices and should almost never be blocked.[15] Since then, antitrust scholars, regulators, and courts have coalesced around a belief that vertical mergers are presumptively procompetitive.[16]

Recently, however, unquestioning acceptance of vertical mergers has started to wane. Increasingly, the evidence suggests that

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[7] *Id.*

[8] *Id.*

[9] *Id.* at 1–2.

[10] *Id.* at 332.

[11] *The Growing Demand for More Vigorous Antitrust Action*, ECONOMIST (Jan 10, 2022), https://www.economist.com/special-report/2022/01/10/the-growing-demand-for-more-vigorous-antitrust-action [https://perma.cc/73FS-JTNR].

[12] *House Antitrust Report*, *supra* note 1, at 332.

[13] JOHN KWOKA, MERGERS, MERGER CONTROL, AND REMEDIES 155 (2014).

[14] Steven C. Salop, *Invigorating Vertical Merger Enforcement*, 127 YALE L.J. 1962, 1964 (2018) ("The last vertical merger case litigated to conclusion by the Federal Trade Commission (FTC) dates back to 1979, which the FTC lost because it was unable to prove probable anticompetitive effects.").

[15] *See infra* Section III.B.

[16] *See infra* Section III.B.

anticompetitive mergers are more likely than the Chicago School believed[17] and that strict adherence to its "consumer welfare standard" misses non-price related harms.[18] European antitrust regulators have largely moved on from the consumer welfare standard, and the U.S. may follow.[19] In 2021, President Biden appointed Lina Khan as Chair of the FTC and Jonathan Kanter to head the DOJ's Antitrust Division, both of whom are well-known Big Tech critics.[20] Recognizing that a lack of modern vertical merger case law is an obstacle, both Agencies have aggressively increased merger challenges under new leadership.[21]

One such challenge concerns Microsoft. In early 2022, the technology conglomerate announced it would acquire Activision Blizzard for $68.7 billion.[22] The proposed merger would vertically integrate Microsoft's Xbox gaming business with one of the largest game studios in the world and the maker of the iconic *Call of Duty* game franchise.[23] Citing concerns that Microsoft would withhold Activision's games from rivals and harm competition, the FTC filed suit to block the merger in December 2022.[24]

This merger challenge is an ideal subject for the ongoing debate surrounding vertical mergers and Big Tech for several reasons. First, Microsoft is one of the largest companies in the world and falls within the family of dominant technology firms that have drawn increasing skepticism from commentators. Next, the video game industry is now the largest entertainment industry in the world, and concentration in this area could significantly affect consumers. At $179.7 billion in 2020 revenue, the video game industry has surpassed the movie, television, and music

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17 *See infra* Section III.C.

18 Lina Khan, *The New Brandeis Movement: America's Antimonopoly Debate*, 9 J. EUR. COMPETITION L. & PRAC. 131, 132 (2018).

19 *The Growing Demand for More Vigorous Antitrust Action*, *supra* note 11.

20 Leah Nylen & Emily Birnbaum, *Biden Picks a Third Trustbuster for His Administration, Putting Big Tech on Notice*, POLITICO (Jul. 20, 2021, 7:12 PM), https://www.politico.com/news/2021/07/20/biden-picks-a-third-trustbuster-for-his-administration-putting-big-tech-on-notice-500310 [https://perma.cc/N7HN-WLYN].

21 Steve Albertson et al., *With Microsoft Complaint, Lina Khan's FTC Takes on Another Big Tech Gaming Deal*, JD SUPRA (Dec. 23, 2022), https://www.jdsupra.com/legalnews/with-microsoft-complaint-lina-khan-s-8091850/ [https://perma.cc/KCK9-2NAY].

22 Cara Lombardo et al., *Microsoft to Buy Activision Blizzard in All-Cash Deal Valued at $75 Billion*, WALL ST. J. (Jan. 18, 2022, 5:49 PM), https://www.wsj.com/articles/microsoft-to-buy-activision-blizzard-games-11642512435?mod=article_inline [https://perma.cc/HRM2-BX7U].

23 *Id.*

24 Press Release, Fed. Trade Comm'n, FTC Seeks to Block Microsoft Corp.'s Acquisition of Activision Blizzard, Inc. Dec. 8, 2022, https://www.ftc.gov/news-events/news/press-releases/2022/12/ftc-seeks-block-microsoft-corps-acquisition-activision-blizzard-inc [https://perma.cc/GNJ9-PEVK].

industries.[25] The industry is also one of the fastest growing, and analysts expect revenues to balloon to $435 billion by 2028.[26] Once dominated largely by young men, the industry has become mainstream with two-thirds of Americans now playing games regularly.[27]

Finally, video games encompass a special business model called platforms. The rise of technology companies has coincided with the rise of platforms.[28] While economists and antitrust attorneys have not reached a consensus on how to define a platform, most agree that they involve two-sided commerce.[29] For example, a video game console is a platform because two sides—video game players and game developers—must participate for the product to succeed. Uber, Airbnb, Google Search, and Facebook are all examples of platforms.[30] The presence of a platform is important in antitrust because platforms face different incentives than traditional firms and may make some anticompetitive conduct more likely.[31]

Surprisingly, little legal scholarship focuses on platform vertical mergers. While many scholars have studied the antitrust implications of platforms,[32] and others have detailed the issues surrounding vertical merger analysis,[33] few have combined the topic.[34] This Article attempts to

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25 Wallace Witkowski, *Videogames are a Bigger Industry than Movies and North American Sports Combined, Thanks to the Pandemic*, MARKETWATCH (Jan. 2, 2021, 10:27 AM), https://www.marketwatch.com/story/videogames-are-a-bigger-industry-than-sports-and-movies-combined-thanks-to-the-pandemic-11608654990 [https://perma.cc/27YP-8ZAS].

26 *Gaming Market Size Worth USD $435 Billion by 2028 | CAGR 12.1%: Zion Market Research*, PR NEWSWIRE (Feb. 14, 2022, 6:30 AM), https://www.prnewswire.com/news-releases/gaming-market-size-worth-usd-435-billion-by-2028--cagr-12-1-zion-market-research-301481456.html [https://perma.cc/Q2JB-4AWF].

27 Marc Saltzman, *More Adults Play Video Games than Kids – And More Surprising Stats*, USA TODAY (Jun. 14, 2022), https://www.usatoday.com/story/tech/gaming/2022/06/11/gaming-study-finds-adults-play-more-than-kids/7581101001/ [https://perma.cc/YU7X-8ZJB].

28 Erik Hovenkamp, *Platform Antitrust*, 44 J. CORP. L. 713, 714 (2018).

29 *Id.* at 720.

30 *Id.* at 714–716.

31 *See infra* Section IV.B.

32 *See*, *e.g.*, David S. Evans, *The Antitrust Economics of Multi-Sided Platform Markets*, 20 YALE J. ON REGUL. 325 (2003); Hovenkamp, *supra* note 28; Michael Katz & Jonathan Sallet, *Multisided Platforms and Antitrust Enforcement*, 127 YALE L.J. 2142 (2018).

33 *See*, *e.g.*, Salop, *supra* note 14; Jonathan M. Jacobson, *Vertical Mergers: Is It Time to Move the Ball*, 33 ANTITRUST 6 (2019); Roger D. Blair et al., *Analyzing Vertical Mergers: Accounting for the Unilateral Effects Tradeoff and Thinking Holistically About Efficiencies*, 27 GEO. MASON L. REV. 761, 761–62 (2020).

34 Bruno Jullien & Wilfred Sand-Zantman, *The Economics of Platforms: A Theory Guide for Competition Policy*, 54 INFO. ECON. & POL'Y, 2021, at 33 ("The literature on mergers of

unify the platform antitrust and vertical merger literature. It does so by using the Microsoft-Activision merger as a case study for evaluating platform vertical mergers.

This Article proceeds as follows. Part II provides background information on the video game industry and the Microsoft-Activision merger. Next, Part III discusses vertical merger law generally. It begins with a brief history of vertical merger law in the U.S. and explains how attitudes towards vertical mergers oscillated over time. Further, this Part explains the current state of vertical merger law after *United States v. AT&T* and discusses the analysis of procompetitive and anticompetitive effects in merger challenges. Part IV introduces basic platform economics and explains how the presence of a platform may make an anticompetitive merger more likely due to indirect network effects. Thereafter, Part V applies these principles to the Microsoft-Activision merger. It argues that Microsoft has a significant incentive to foreclose rivals from Activision's content and that the merger's anticompetitive effects could harm consumers and rivals. This analysis has important implications for future platform vertical merger challenges. Part VI concludes.

II. VIDEO GAME INDUSTRY BACKGROUND

A. *The Video Game Industry*

The video game console industry is dominated by three companies—Sony's PlayStation, Microsoft's Xbox, and Nintendo's Switch (hereafter the "Big 3").[35] Each of these companies designs, manufactures, and distributes consoles. Nintendo, the oldest of the three, has carved out a separate niche focusing on a portable gaming experience. Consumers who own a Switch can play their games in the handheld mode or place it in a dock that connects to their televisions.[36] By contrast, Sony and Microsoft focus on a more "traditional" gaming experience where consumers play games only on a television through a much larger console that resembles a desktop computer.[37] PlayStation and Xbox possess superior computing power over the Switch due to the Switch's focus on

platform is still in its infancy, due to the difficulty of modeling multi-platform competition.").

35 Arthur Gies & Haley Perry, *The Best Game Consoles*, N.Y. TIMES | WIRECUTTER (Feb. 10, 2023), https://www.nytimes.com/wirecutter/reviews/best-game-consoles/ [https://perma.cc/7LZF-3STT].

36 *Nintendo Switch: Features Comparison*, NINTENDO, https://www.nintendo.com/switch/compare/ [https://perma.cc/PS7H-LQ5R].

37 Gies & Perry, *supra* note 35.

portable gaming.[38] Accordingly, PlayStation and Xbox are often viewed as more direct competitors and operate in a subniche of console gaming that the FTC dubs "high-performance" gaming.[39] Even though the Switch cannot handle the more technologically demanding games of its competitors, many games are released across all three consoles, forming a general video game console market.[40]

Integral to the console market, developers and publishers supply games to consumers. Developers undertake the creative task of designing and programming a game, while publishers market and distribute them (collectively referred to as "studios").[41] Each of the Big 3 also operates their own in-house gaming studios, which develop games for exclusive use on their own consoles.[42] Independent studios may make games for any of the Big 3 consoles but often form agreements to offer certain games exclusively to one console.[43] These *exclusive titles* are strategically important for the Big 3 and the studios alike because they impact both development costs and revenue.[44]

The video game industry has its own version of "blockbusters" known as *AAA games*.[45] Like their movie analogs, AAA games have multi-million-dollar budgets, take years to develop, and have high earnings potential.[46] For example, the top movie of 2022, *Top Gun: Maverick*, grossed $1 billion at the box office in 30 days.[47] Comparatively, the latest installment of the *Call of Duty* franchise was released in late 2022 and earned that same number in just 10 days.[48] AAA games are extremely important to the industry because they represent a small fraction of all games but produce most of the revenue.[49] A single AAA game can

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38 *Id.*

39 Admin. Part 3 Complaint (Redacted Pub. Version) at 2, In re Microsoft Corp., No. 9412 (F.T.C., Dec. 8, 2022) [hereinafter *FTC Complaint*].

40 Gies & Perry, *supra* note 35.

41 Robin S. Lee, *Vertical Integration and Exclusivity in Platform and Two-Sided Markets*, 103 AM. ECON. REV. 2960, 2965 (2013).

42 *Id.*

43 *Id.*

44 *Id.*

45 Pronounced "triple A."

46 *Why Video Games Are So Expensive to Develop*, ECONOMIST (Sep. 25, 2014), https://www.economist.com/the-economist-explains/2014/09/24/why-video games-are-so-expensive-to-develop [https://perma.cc/KP6D-6TMJ].

47 *Microsoft, Activision Blizzard and the Future of Gaming*, ECONOMIST (Nov. 29, 2022), https://www.economist.com/business/2022/11/29/microsoft-activision-blizzard-and-the-future-of-gaming [https://perma.cc/4KFY-7CZY].

48 *Id.*

49 Ricard Gil & Frederic Warzynski, *Vertical Integration, Exclusivity, and Game Sales Performance in the US Video Game Industry*, 31 J.L., ECON., & ORG. i143, i150 (2014).

convince a consumer to spend hundreds of dollars on a console.[50] Some AAA games like *Call of Duty* are available on multiple consoles while others like Sony's *God of War*[51] are only available on one.[52] Securing exclusive access to one of these games has significant business implications.[53] Due to the immense cost and time requirements, few large studios possess the resources to create AAA games.[54] In addition to each of the Big 3, AAA-capable studios include Activision Blizzard, Tencent, Electronics Arts (EA), Bandai Namco, Take-Two Interactive, and Ubisoft.[55]

B. *Microsoft-Activision Merger*

Microsoft announced it would acquire Activision Blizzard in January 2022.[56] Valued at $68.7 billion, the proposed merger is Microsoft's and the video game industry's largest ever.[57] The acquisition came just over a year after Microsoft completed the acquisition of another sizeable video game studio, ZeniMax Media, for $7.5 billion.[58] Merging with Activision Blizzard would create the third largest gaming company in the world[59] and add to Microsoft's sizable portfolio of gaming content.[60] This merger is

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50 Haeyop Song et al., *Platform Competition in the Video Game Console Industry: Impacts of Software Quality and Exclusivity on Market Share*, 30 J. MEDIA ECON. 99, 101 (2018).

51 *God of War: Ragnarök* was the fourth highest grossing game of 2022. Tom Ivan, *NPD Has Revealed the Best-Selling Games of 2022 in the United States*, VIDEO GAMES CHRON. (Jan. 16, 2023, 4:17 PM), https://www.videogameschronicle.com/news/npd-has-revealed-the-best-selling-games-of-2022-in-the-united-states/ [https://perma.cc/YPY9-Y5C6].

52 *Microsoft, Activision Blizzard and the Future of Gaming*, *supra* note 47.

53 *See infra* Section V.B.1.

54 COMPETITION & MKTS. AUTH., ANTICIPATED ACQUISITION BY MICROSOFT OF ACTIVISION BLIZZARD, INC.: FINAL REPORT 40 (Apr. 26, 2023) [hereinafter CMA, FINAL REPORT], https://assets.publishing.service.gov.uk/media/644939aa529eda000c3b0525/Microsoft_Activision_Final_Report_.pdf [https://perma.cc/62P8-BXXF].

55 Devin Pickell, *The 13 Most Prominent Video Game Publishers in the World*, G2 (Oct. 30, 2019), https://learn.g2.com/video-game-publishers [https://perma.cc/DF7B-QTES].

56 Press Release, Microsoft to Acquire Activision Blizzard to Bring the Joy and Community of Gaming to Everyone, Across Every Device, Microsoft (Jan. 18, 2022), https://news.microsoft.com/2022/01/18/microsoft-to-acquire-activision-blizzard-to-bring-the-joy-and-community-of-gaming-to-everyone-across-every-device/ [https://perma.cc/6X9F-7JZW].

57 Cara Lombardo et al., *supra* note 22.

58 Aaron Tilley & Sara E. Needleman, *Microsoft to Buy Doom Owner in $7.5 Billion Videogames Deal*, WALL ST. J. (Sep. 1, 2021, 1:51 PM), https://www.wsj.com/articles/microsoft-to-buy-videogame-maker-zenimax-media-for-7-5-billion-11600697758 [https://perma.cc/4LMF-8NA3].

59 Press Release, *supra* note 56.

60 Tilley & Needleman, *supra* note 58.

part of a wider trend of consolidation currently underway in the video game industry.[61]

1. The Parties

Microsoft is one of the world's largest technology companies and consistently ranks among its most valuable.[62] Founded in 1975, the company quickly became synonymous with computers and was made famous by its Windows Operating System, Office suite, and Internet Explorer.[63] It entered the video game industry with the launch of the original Xbox in 2001 and has since released three upgraded versions—the Xbox 360, Xbox One, and Xbox Series X/S.[64] Microsoft creates its own games under its Xbox Game Studios division, which encompasses 23 developers and produces popular game franchises such as *Halo*, *Doom*, *Microsoft Flight Simulator*, *Minecraft*, *Fallout*, and *The Elder Scrolls*.[65] Further, Microsoft operates Xbox Game Pass, a subscription- and cloud-based gaming service.[66] In addition to video games, Microsoft has entered the markets for cloud computing, online search, artificial intelligence, and others.[67]

Activision was founded in 1979 when three employees left Atari over creative rights in video games.[68] Activision quickly grew into a successful gaming company and is responsible for popular titles such as *Guitar Hero*, *Crash Bandicoot*, *Spyro the Dragon*, and *Tony Hawk's Pro Skater*.[69]

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[61] *See generally* Clayton Alexander, *Game Over? How Video Game Console Makers Are Speeding Toward an Antitrust Violation*, 4 BUS. ENTREPRENEURSHIP & TAX L. REV. 151 (2020) (describing consolidation in industry); *see also* Shannon Liao & Nathan Grayson, *Microsoft and Sony Are Buying Up the Video Game World. The FTC Could Stop Them.*, WASH. POST (Feb. 8, 2022, 4:06 PM), https://www.washingtonpost.com/video-games/2022/02/08/why-microsoft-buy-activision-sony-bungie/ [https://perma.cc/CQZ6-A7GY].

[62] In 2022, Microsoft was the world's second most valuable company by market capitalization at $2.311 trillion. Gary Hoover, *Most Valuable U.S. Companies 1995 Through 2022*, AM. BUS. HIST. CTR. (Jul. 8, 2022), https://americanbusinesshistory.org/most-valuable-u-s-companies-1995-through-2022/ [https://perma.cc/U5XJ-KUTC]. At various points over the last 25 years, it has been the most valuable. *Id.*

[63] *See Microsoft Corporation*, BRITANNICA, https://www.britannica.com/topic/Microsoft-Corporation [https://perma.cc/7USX-2NJG] (last updated Aug. 28, 2023) (describing Microsoft's history).

[64] *Id.*

[65] *Xbox Game Studios*, MICROSOFT, https://www.xbox.com/en-US/xbox-game-studios [https://perma.cc/G7UA-F45K].

[66] For more details, see *infra* Section II.C.

[67] *Microsoft Corporation*, *supra* note 63.

[68] *Activision Blizzard, Inc.*, BRITANNICA, https://www.britannica.com/topic/Activision-Blizzard-Inc [https://perma.cc/5J4W-EJX7] (last updated Feb 21, 2023).

[69] *Id.*

Originally a separate studio, Blizzard Entertainment was founded in 1991 and is most known for *World of Warcraft*, *Diablo*, and *Overwatch*.[70] In 2008, the companies merged, forming Activision Blizzard.[71] The combined company is one of the largest game studios in the world by revenue.[72] Famously, Activision Blizzard created *Call of Duty*, one of the most successful gaming franchises of all time, which has generated over $30 billion in lifetime revenue.[73]

2. Merger Challenges

The FTC sued to block the merger under Section 7 of the Clayton Act in its Administrative Law Court on December 8, 2022.[74] The agency alleged that the merger would substantially lessen competition because Microsoft would have the ability and incentive to withhold or degrade content from rivals.[75] It argued the result of such conduct could raise rivals' costs, increase barriers to entry, stifle competition and innovation, and reduce quality in the market for consoles and cloud streaming.[76] Microsoft denied these allegations and argued the merger will result in procompetitive efficiencies that will benefit consumers.[77]

Global regulators also launched merger investigations.[78] Notably, the United Kingdom's Competition and Market's Authority ("CMA") blocked the merger in April 2023, finding that the deal would likely result

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[70] *Id.*
[71] *Id.*
[72] Pickell, *supra* note 55.
[73] Mike Hume, *The Future of Call of Duty and 'Warzone'*, WASH. POST (June 8, 2022, 1:00 PM), https://www.washingtonpost.com/video-games/2022/06/08/call-duty-future-modern-warfare-2-warzone-2/ [https://perma.cc/4TAY-GJVX].
[74] *FTC Complaint*, *supra* note 39, at 21–23.
[75] *Id.* at 17–20.
[76] *Id.*
[77] Amended Answer and Def. of Respondent Microsoft Corp. at 32, In re Microsoft Corp., No. 9412 (F.T.C., Jan. 24, 2023) [hereinafter *Microsoft Answer*].
[78] *See Microsoft / Activision Blizzard Merger Inquiry*, COMPETITION & MKTS. AUTH., https://www.gov.uk/cma-cases/microsoft-slash-activision-blizzard-merger-inquiry (last visited Feb. 16, 2023); Press Release, Mergers: Commission Opens In-Depth Investigation into the Proposed Acquisition of Activision Blizzard by Microsoft, Eur. COMM'N (Nov. 8, 2022), https://ec.europa.eu/commission/presscorner/detail/en/ip_22_6578 [https://perma.cc/66Z4-KPAN].

"in [a substantial lessening of competition] in cloud gaming services in the UK."[79] Microsoft appealed that decision.[80]

In June 2023, the FTC filed a preliminary injunction in the Northern District of California to prevent Microsoft and Activision from closing the deal before it could hold administrative hearings.[81] The court denied the FTC's request, holding that the FTC failed to show the merger would substantially lessen competition in the video game industry.[82] The same day, the CMA signaled a willingness to reexamine the merger and agreed to pause the appeal pending in the UK for further negotiations.[83]

With only the CMA left to convince, Microsoft restructured the merger by selling the game streaming rights for all existing and new Activision games for the next 15 years to rival game studio and streamer, Ubisoft.[84] The CMA found that the restructured deal amounted to a material change of circumstances that would alleviate its concerns over other game streamers' ability to compete in the market and approved the deal.[85] Microsoft and Activision finalized the merger on October 13, 2023.[86]

C. *The "Streamification" of Video Games*

The future of video games is subscription-based streaming. A race to become the "Netflix of games" is underway and Microsoft currently

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79 CMA, FINAL REPORT, *supra* note 54, at 4–6.

80 Sam Tobin, *Microsoft Sets Out Grounds for Activision Appeal Against UK Regulator*, REUTERS (May 26, 2023, 2:08 PM), https://www.reuters.com/markets/deals/microsoft-sets-out-activision-appeal-against-uk-regulator-2023-05-26/ [https://perma.cc/GE9X-58VW].

81 FTC v. Microsoft Corp., No. 23-cv-02880-JSC, 2023 WL 4443412, at *1 (N.D. Cal. Jul. 10, 2023).

82 *Id.*

83 Sam Tobin & Paul Sandle, *Microsoft Granted Two-Month Pause of UK Appeal Over Activision Deal*, REUTERS (July 17, 2023, 1:45 PM), https://www.reuters.com/markets/deals/microsoft-uk-ask-two-month-pause-appeal-over-activision-deal-2023-07-17/ [https://perma.cc/44G9-4ZJT].

84 Kate Holton & Paul Sandle, *Microsoft, Activision to Sell Streaming Rights to Secure Biggest Video Gaming Deal*, REUTERS (Aug. 22, 2023 12:44 PM), https://www.reuters.com/technology/uk-opens-new-probe-into-microsofts-purchase-activision-2023-08-22/ [https://perma.cc/RN9W-UKD7].

85 COMPETITION & MKTS. AUTH., ANTICIPATED ACQUISITION BY MICROSOFT CORPORATION OF ACTIVISION BLIZZARD (EXCLUDING ACTIVISION BLIZZARD'S NONEEA CLOUD STREAMING RIGHTS) 7–8 (Oct. 13, 2023), https://assets.publishing.service.gov.uk/media/652864062548ca000dddf22d/Full_text_decision__final_order_.pdf [https://perma.cc/2JLG-LLKC].

86 Tom Dotan & Sarah E. Needleman, *Microsoft's Activision Buy Extends Nadella's Decade of Deals*, WALL. ST. J. (Oct. 13, 2023 12:17 PM), https://www.wsj.com/tech/microsofts-activision-deal-gets-green-light-from-u-k-regulator-95fd688a [https://perma.cc/H3A6-M4E7].

leads.[87] Microsoft launched its subscription gaming service, Game Pass, in 2017, and the company had reported 25 million subscribers by 2022.[88] For $10–$17 per month, subscribers to Game Pass can play any game within the service's library.[89] In 2022, Microsoft became the first of the Big 3 to launch a pure game streaming service with the introduction of the Xbox TV app.[90] With it, subscribers can stream games directly to their TV, no console required.[91]

Similarly, Sony launched its gaming subscription service, PlayStation Now, in 2014.[92] Recently, Sony discontinued PlayStation Now to better compete with Microsoft.[93] Instead, it now offers a similar service under the highest tier of its PlayStation Plus subscription.[94] Until recently, Nintendo did not offer subscription-based access to its game catalog, but

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87 CMA, FINAL REPORT, *supra* note 54, at 4, 8, 294 ("In relation to cloud gaming services, we found that Microsoft already has a strong position. It owns a popular gaming platform (Xbox and a large portfolio of games), the leading PC operating system (Windows), and a global cloud computing infrastructure (Azure and Xbox Cloud Gaming), giving it important advantages in running a cloud gaming service. With an estimated 60-70% market share in global cloud gaming services, it is already much stronger than its rivals[,]" and "cloud gaming may be an important disruptive force in the gaming industry."); *see also Netflix, but for Video Games*, ECONOMIST (Feb. 2, 2019) https://www.economist.com/business/2019/02/02/netflix-but-for-video-games [https://perma.cc/HHE2-CARJ].

88 Sarah E. Needleman, *Sony's Expanded PlayStation Plus Subscription Aims to Take on Xbox Game Pass*, WALL ST. J. (Mar. 29, 2022), https://www.wsj.com/articles/sony-to-fold-playstation-now-into-its-online-multiplayer-service-for-console-customers-11648567465 [https://perma.cc/27AX-LYR9].

89 *Xbox Game Pass*, XBOX, https://www.xbox.com/en-US/xbox-game-pass?xr=shellnav [https://perma.cc/76C6-7JTM].

90 Aisha Malik, *Microsoft's New Xbox TV App Will Let Player's Stream Games on New Samsung Smart TVs Without a Console*, TECHCRUNCH (Jun. 9, 2022, 9:11 AM), https://techcrunch.com/2022/06/09/microsofts-xbox-tv-app-stream-games-new-samsung-smart-tvs/ [https://perma.cc/JC7M-KK6F].

91 *Id.*

92 Michael Higham, *PS Now Explained: What You Need to Know About Sony's Cloud Gaming Service*, GAMESPOT (Jan. 11, 2022), https://www.gamespot.com/articles/ps-now-explained-what-you-need-to-know-about-sonys-cloud-gaming-service/1100-6471137/ [https://perma.cc/NN8A-MF42].

93 Needleman, *supra* note 88.

94 For many years, PlayStation Plus coexisted with PlayStation Now. While PlayStation Now offered subscription-based access to a game library, PlayStation Plus primarily offered access to multiplayer online gaming and discounts on games. The equivalent of PlayStation Now can now be obtained by purchasing a PlayStation Plus Premium subscription. For more information, see *Update: Your Guide to the All-New PlayStation Plus*, PLAYSTATION.BLOG (May 23, 2022), https://blog.playstation.com/2022/05/23/your-guide-to-the-all-new-playstation-plus/ [https://perma.cc/LE7T-5K73].

in October 2021, it launched Nintendo Switch Online + Expansion Pack, which provides access to Nintendo 64 and SEGA Genesis games.[95]

The subscription-based gaming model is not exclusive to the Big 3. Big-Tech (Amazon, Google, Meta, and Apple), game developers (Electronic Arts and Ubisoft), television streaming companies (Netflix), startups (Utomik and Blacknut), and even a semiconductor company (Nvdia) have all launched subscription gaming services. Notably, Amazon's Luna and Google's Stadia are pure game streaming services, akin to a "Netflix of games."[96] As the video game industry turns to streaming, the Microsoft-Activision merger may have substantial ramifications on the trajectory of this nascent industry.

III. ANTITRUST VERTICAL MERGER LAW

This Part traces the evolution of vertical merger law in the United States beginning with the pre-1950 period when vertical merger challenges were almost non-existent. Then, in 1950, challenges to vertical mergers substantially increased following amendments to the Clayton Act that explicitly allowed for challenges to vertical mergers. By the late 1970s, the Chicago School's influence over antitrust laws led to the current procompetitive views of vertical mergers. Finally, vertical mergers have recently received renewed attention with the rise of Big Tech and the DOJ's high-profile merger challenge in *United States v. AT&T*.

A. *A Brief History of Antitrust Merger Law*

American industry underwent rapid consolidation in the late 19th century, enabled by two novel legal inventions. First, a Standard Oil attorney invented the trust, which vested control of independent companies within a particular industry to a group of trustees who could fix output and pricing.[97] Second, New Jersey enacted the country's first

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[95] Adam Bankhurst, *Nintendo Switch Online + Expansion Pack Is Now Live*, IGN (Oct. 26, 2021), https://www.ign.com/articles/nintendo-switch-online-expansion-pack-release-date-pricing-n64-sega-games [https://perma.cc/X3GP-G99J].

[96] *See* Aaron Tilley, *Microsoft's Videogame Boss and the Long Battle to Reinvent the Company*, WALL ST. J. (Feb. 4, 2022, 12:15 PM), https://www.wsj.com/articles/microsofts-videogame-boss-and-the-long-battle-to-reinvent-the-company-11643912561?mod=article_inline [https://perma.cc/DML7-QD6F] (describing Microsoft's ambition to become a "Netflix for gaming"); *Netflix, but for Video Games*, *supra* note 87.

[97] DIANE TELGEN, DEFINING MOMENTS: THE GILDED AGE 46 (2012); Laura Phillips Sawyer, *US Antitrust Law and Policy in Historical Perspective* 2 (Harv. Bus. Sch., Working Paper No. 19–110, 2019), https://www.hbs.edu/ris/Publication%2520Files/19-110_e21447ad-d98a-451f-8ef0-ba42209018e6.pdf [https://perma.cc/9N3S-JBAT].

holdings corporation legislation, which made it legal to own corporations across state lines and led to a plethora of mergers.[98] The "Great Merger Movement" of the late 19th century saw 1800 firms consolidate down to 160, with one-third of those firms controlling 70% of their respective market and half controlling at least 40 percent.[99]

Against this backdrop, Congress passed the Sherman Antitrust Act in 1890 as "a comprehensive charter of economic liberty aimed at preserving free and unfettered competition as the rule of trade."[100] Section 2 of the Sherman Act prohibits monopolization or attempted monopolization of "any part of the trade or commerce among the several States."[101] A party can challenge vertical conduct constituting monopolization or attempted monopolization under Section 2.[102]

The Sherman Act lacked teeth for over a decade until Theodore Roosevelt assumed the presidency.[103] Between Presidents Roosevelt and Taft, their administrations prosecuted 120 antitrust cases and confronted industry titans such as Standard Oil, U.S. Steel, and AT&T.[104] Despite aggressive enforcement, monopolists successfully circumvented the Sherman Act through mergers.[105] In response, President Wilson signed into law the Clayton Antitrust Act in 1914.[106] Section 7 of the Clayton Act prohibits a merger if its effect "may be substantially to lessen competition, or to tend to create a monopoly."[107] President Wilson further bolstered antitrust enforcement with the passage of the Federal Trade Commission Act, which created the FTC and enabled it to regulate mergers and anticompetitive conduct.[108]

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98 JERRY W. MARKHAM, A FINANCIAL HISTORY OF THE UNITED STATES: FROM CHRISTOPHER COLUMBUS TO THE ROBBER BARONS (1492–1900), at 356–57 (2002).
99 Naomi R. Lamoreaux, *The Problem of Bigness: From Standard Oil to Google*, 33 J. ECON. PERSPS. 94, 98 (2019).
100 N. Pac. Ry. Co. v. United States, 356 U.S. 1, 4 (1958).
101 15 U.S.C. § 2.
102 Lina M. Khan, *The Separation of Platforms and Commerce*, 119 COLUM. L. REV. 973, 1024–25 (2019).
103 TIM WU, THE CURSE OF BIGNESS: ANTITRUST IN THE NEW GILDED AGE 46–48 (2018).
104 *Id.* at 74.
105 Wiliam E. Kovacic, *Failed Expectations: The Troubled Past and Uncertain Future of the Sherman Act as a Tool for Deconcentration*, 74 IOWA L. REV. 1105, 1124 (1989).
106 TELGEN, *supra* note 97, at 116.
107 15 U.S.C. § 18.
108 Andrea Koutsoudakis, *Antitrust More than a Century After Sherman: Why Protecting Competitors Promotes Competition More than Economically Efficient Mergers*, 34 U. DAYTON L. REV. 223, 237 (2009).

B. *How Attitudes Towards Vertical Mergers Evolved*

There are two types of mergers: horizontal and vertical. A horizontal merger occurs when two companies join that directly compete with one another by selling the same product.[109] In contrast, vertical mergers occur when two companies join along different parts of the same supply chain.[110] Horizontal mergers receive greater scrutiny, and scholars generally agree that they pose a greater threat to competition because the combined firm has the ability and incentive to raise prices, thereby harming consumers.[111] Unlike horizontal mergers, the leading consensus today is that vertical mergers are usually procompetitive because they create cost savings that benefit consumers through lower prices.[112] Accordingly, they receive less scrutiny than horizontal mergers.[113] Indeed, the DOJ's suit against AT&T in 2017 challenging its acquisition of Time Warner was the first vertical merger litigated in almost 40 years.[114] However, the Agencies have not always been so friendly to vertical mergers, and for many decades courts presumed vertical mergers were anticompetitive.

Before antitrust enforcement, vertical and horizontal mergers harmed American consumers. For example, Standard Oil dominated the oil industry by the early 1900s through horizontal mergers where it acquired direct competitors, leading to its eventual break up into 34 distinct companies.[115] Alternatively, Carnegie Steel pursued dominance through vertical integration, acquiring a presence in every step of the steel-

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109 U.S. DEPT'T OF JUST. & FED. TRADE COMM'N, HORIZONTAL MERGER GUIDELINES, at 1 (2010), https://www.ftc.gov/sites/default/files/attachments/mergers/100819hmg.pdf [https://perma.cc/8D3D-HQVC].

110 *See Competitive Effects*, FED. TRADE COMM'N, https://www.ftc.gov/advice-guidance/competition-guidance/guide-antitrust-laws/mergers/competitive-effects [https://perma.cc/GQX5-TWUS] ("Vertical mergers involve firms in a buyer-seller relationship — for example, a manufacturer merging with a supplier of an input product, or a manufacturer merging with a distributor of its finished products.").

111 Blair et al., *supra* note 33, at 763, 766–67; *see also Mergers*, FED. TRADE COMM'N, https://www.ftc.gov/advice-guidance/competition-guidance/guide-antitrust-laws/mergers [https://perma.cc/V2SB-78E6] ("The greatest antitrust concern arises with proposed mergers between direct competitors (horizontal mergers).").

112Blair et al., *supra* note 33, at 761–62.

113 *Id.* at 761–62.

114 *Id.* at 764; *see also* United States v. AT&T, Inc., 310 F. Supp. 3d 161, 193–94 (D.D.C. 2018), *aff'd*, 916 F.3d 1029 (D.C. Cir. 2019).

115 *See* Koutsoudakis, *supra* note 108, at 234–35 (describing Standard Oil's horizontal mergers); WU, *supra* note 103, at 63–67 (2018) (describing Standard Oil's anticompetitive practices and eventual breakup).

making process.[116] Such integration granted Carnegie superior cost efficiency, which allowed it to routinely slash prices to levels competitors could not match and then raise them again once the competitor left the market.[117]

Initially, the Agencies believed that the Clayton Act did not extend to vertical mergers.[118] Instead, the Agencies used the Clayton Act to prevent the creation of trusts such as Standard Oil through horizontal mergers.[119] While the Agencies investigated vertical mergers, they rarely pursued action and recommended Congress modify the Clayton Act to cover vertical mergers.[120] Opponents of vertical mergers argued that companies may harm competition through "leverage" by using their market power to make it more difficult for rivals to enter a market or "foreclosure" by depriving competitors from accessing the goods of the acquired firm.[121] Supreme Court Justice Louis Brandeis, an influential antitrust thought leader in his lifetime, argued that the concentration of wealth in too few corporations was a threat to democracy itself.[122]

The Agencies finally got their wish in 1950. After World War II, American corporations underwent another period of rapid consolidation, and Congress responded by passing the Celler-Kefauver Act of 1950, amending the Clayton Act to specifically account for vertical mergers.[123] Echoing Justice Brandeis, members of Congress passed the amendments to curb the concentration of economic power in the hands of a few large corporations.[124] Following the Act's passage, the Agencies successfully challenged many vertical mergers, which were almost always viewed as anticompetitive.[125] The Supreme Court also viewed vertical mergers with skepticism writing in *Brown Shoe Co. v. United States* that "by foreclosing the competitors of either party from a segment of the market otherwise open to them, the [vertical] arrangement may act as a 'clog on competition'" and "deprive[] . . . rivals of a fair opportunity to compete."[126]

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[116] TELGEN, *supra* note 97, at 48.
[117] *Id.* at 48–49.
[118] Blair et al., *supra* note 33, at 799–800.
[119] *Id.* at 802.
[120] *Id.* at 803–04.
[121] Khan, *supra* note 102, at 1020–21.
[122] Carl T. Bogus, *The New Road to Serfdom: The Curse of Bigness and the Failure of Antitrust*, 49 U. MICH. J.L. REFORM 1, 2–3, 68 (2015).
[123] *Id.* at 74.
[124] *Id.* at 75.
[125] Blair et al., *supra* note 33, at 800.
[126] Brown Shoe Co. v. United States, 370 U.S. 294, 324 (1962) (first quoting Standard Oil Co. of Calif. v. United States, 337 U.S. 293, 314 (1949); then quoting H.R.REP. NO. 1191, at 8 (1949)).

However, the rise of the Chicago School in the 1970s reversed vertical merger enforcement policy and remains the leading consensus view today. The Chicago School of Economics originated at the University of Chicago and advanced economic theories underpinned by free-enterprise and limited government.[127] Its theories spilled over into law and heavily influenced antitrust.[128] Famously, former U.S. Attorney General Robert Bork authored *The Antitrust Paradox: A Policy at War with Itself* where he argued that "[t]he only legitimate goal of antitrust law is the maximization of consumer welfare."[129] He further argued that antitrust law should ignore vertical mergers because they almost always increase efficiency.[130] Vertical mergers eliminate redundant costs and allow firms to simultaneously increase their profits and lower their prices, thereby increasing general and consumer welfare.[131] Thus, the "consumer welfare standard" was born, and courts became hyper-focused on how alleged anticompetitive conduct affected the ultimate prices paid by consumers.[132] These theories upended previous thinking on vertical mergers, which are now presumed to be procompetitive.[133]

While the consumer welfare standard and default assumptions about the procompetitive nature of vertical mergers predominate current antitrust law, a growing concentration of wealth in a few firms, particularly large tech firms, has sparked renewed interest in antitrust law reform.[134] New Brandeisians, named for Justice Brandeis, view this concentration of wealth and power with skepticism.[135] They argue that the consumer welfare standard's focus on maintaining lower prices misses other anticompetitive harms and antitrust law should evolve to account for them.[136]

After regulators and courts embraced the Chicago School, vertical merger enforcement disappeared. In 2017, the Justice Department's challenge of the AT&T-Time Warner merger became the first vertical

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127 H. Laurence Miller, *On the "Chicago School of Economics"*, 70 J. POL. ECON. 64, 64–65 (1962).
128 Bogus, *supra* note 122, at 27.
129 *Id.* at 16 (quoting ROBERT H. BORK, THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF 51 (1978)).
130 *Id.* at 21.
131 Blair et al., *supra* note 33, at 768–69.
132 Khan, *supra* note 18, at 132.
133 Khan, *supra* note 102, at 1023–24.
134 David McCabe & Steve Lohr, *Congress Faces Renewed Pressure to 'Modernize our Antitrust Laws'*, N.Y. TIMES (Jun. 29, 2021), https://www.nytimes.com/2021/06/29/technology/facebook-google-antitrust-tech.html [https://perma.cc/TCA9-6GNS].
135 Khan, *supra* note 18, at 131.
136 *Id.* at 132.

merger litigated by either antitrust agency in nearly 40 years.[137] Empirical evidence suggests that current standards have resulted in significant merger underenforcement with the Agencies acting in only 38% of mergers that resulted in price increases for consumers.[138] As part of the ongoing debate over antitrust reform, some scholars have advocated for a return to more vigorous merger enforcement.[139] However, antitrust regulators face a dilemma in that they have no modern precedent from which to launch a successful challenge. In *AT&T*, the court itself acknowledged a "dearth of authority" on which to base its decision.[140] In response, the Agencies have pursued more aggressive merger enforcement[141] to establish new case law.[142] The FTC's challenge of the Microsoft-Activision merger was among the first to litigate a Big Tech vertical merger.[143]

C. *Current Vertical Merger Analysis*

In 2016, AT&T announced its acquisition of Time Warner for $108 billion.[144] The merger sought to vertically integrate AT&T's pay-TV services with Time Warner's suite of entertainment content including Warner Bros., Turner's cable TV networks, and HBO.[145] Citing concerns that the merger would raise rivals' costs for Time Warner's content and harm consumers, the DOJ filed suit under Section 7 of the Clayton Act to block the merger.[146]

Confronted with the first vertical merger challenge in four decades, the District Court for the District of Columbia turned to

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137 United States v. AT&T, Inc., 310 F. Supp. 3d 161, 193–94 (D.D.C. 2018), *aff'd*, 916 F.3d 1029 (D.C. Cir. 2019).
138 KWOKA, *supra* note 13, at 155.
139 *See generally* Salop, *supra* note 14 (arguing for more vigorous vertical merger enforcement).
140 *AT&T*, 310 F. Supp. 3d at 193–94.
141 Rebecca Farrington & Heather Greenfield, *Antitrust Scrutiny Intensifies as DOJ and FTC Step Up Enforcement*, WHITE & CASE (Jan. 27, 2023), https://www.whitecase.com/insight-our-thinking/us-ma-fy-2022-antitrust-scrutiny-intensifies [https://perma.cc/5N3G-J428].
142 Brent Kendall & Dave Michaels, *Microsoft Case Poses Crucial Test for FTC's Fight Against 'Vertical' Mergers*, WALL ST. J. (Dec. 9, 2022, 3:24 PM), https://www.wsj.com/articles/microsoft-case-poses-crucial-test-for-ftcs-fight-against-vertical-mergers-11670617455 [https://perma.cc/M3T7-9TS7] ("There is less case law to support vertical-merger challenges, but the FTC and Justice Department can only change that by taking more cases to court.") (quoting former DOJ official Barry Nigro).
143 *Id.* (describing other cases brought by the Agencies).
144 *AT&T*, 310 F. Supp. 3d at 164.
145 *Id.* at 177–78.
146 *Id.* at 164.

horizontal merger case law for guidance and adopted the burden-shifting framework from *United States v. Baker Hughes*.[147] The *Baker Hughes* framework provides a three-part burden-shifting test: (1) the government first must show the merger will substantially lessen competition in the relevant product and geographic market; (2) then the burden shifts to the Defendant to either disprove the government's argument or show that "efficiencies outweigh the merger's anticompetitive effects"; and (3) in the final step, the burden shifts back to the government to further support evidence of anticompetitive effects, which "merges with the government's ultimate burden of persuasion."[148] Unlike horizontal mergers where the government can show anticompetitive effects by demonstrating the merger increases market concentration, the court noted vertical mergers have no comparable "short-cut" on the first prong because vertical mergers do not change market share.[149] Thus, the court concluded that the government bears the initial burden of establishing that the merger will likely create anticompetitive effects through "case-specific evidence."[150]

Given the lack of modern vertical merger litigation precedent, *AT&T* provides the best indication of how courts will treat vertical mergers. On appeal, the D.C. Circuit noted that several amici curiae urged the court to articulate the proper standard for vertical mergers.[151] However, it declined to do so because neither party challenged the application of the *Baker Hughes* framework.[152] While the court's dicta signaled an openness to an alternative test, most antitrust scholars agree that the general framework should apply.[153] Further, in considering the FTC's preliminary injunction against the Microsoft-Activision merger, the Northern District of California also embraced the approach taken in *AT&T* and adopted the *Baker Hughes* framework for vertical mergers.[154] Accordingly, this Article assumes that future vertical merger challenges will apply the *Baker Hughes* framework as articulated in *AT&T*.

In applying the *Baker Hughes* framework, much of the litigation turns on a comparison of the merger's predicted procompetitive and anticompetitive effects. Vertical mergers often create both procompetitive and anticompetitive effects.[155] Generally, there is a strong procompetitive

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147 *Id.* at 190–91.
148 *Id.* at 191 (citing United States v. Baker Hughes Inc., 908 F.2d 981, 991 (D.C. Cir. 1990)).
149 *Id.* at 192.
150 *Id.* at 194.
151 United States v. AT&T, Inc., 916 F.3d 1029, 1037 (D.C. Cir. 2019).
152 *Id.* at 1037.
153 Jacobson, *supra* note 33, at 10.
154 FTC v. Microsoft Corp., No. 23-cv-02880-JSC, 2023 WL 4443412, at *8, *11–12 (N.D. Cal. Jul. 10, 2023).
155 Blair et al., *supra* note 33, at 792.

assumption for vertical mergers because procompetitive efficiencies will usually outweigh the negative effects flowing from the merger.[156] In *AT&T*, the court acknowledged the difficulty the DOJ faced in overcoming these assumptions.[157] Further, empirical evidence reveals that most vertical mergers have benefitted consumers.[158] However, a growing contingent of antitrust scholars and regulators argue that such generalizations about vertical mergers are overbroad, and procompetitive effects are never guaranteed.[159] Courts are receptive to this idea, and in *AT&T*, the district court acknowledged "that vertical mergers 'are not invariably innocuous.'"[160]

The remainder of this Section describes the range of procompetitive and anticompetitive effects attorneys and their economists use to show whether a merger will substantially lessen competition. As part of the discussion on procompetitive effects, it examines the ongoing debate on default assumptions and discusses situations where procompetitive vertical mergers may not always arise. Further, the following Sub-Sections examine the typical criticisms of anticompetitive theories of harm and discuss the evidence showing that anticompetitive harms are more likely to arise than some would predict.

1. Procompetitive Effects

Primarily, vertical mergers benefit competition through various efficiencies that result when firms combine. Examples of efficiencies include reductions in transaction costs and asymmetric risk, knowledge, information, and experience-sharing benefits, inventory cost synergies, and others.[161]

The most prominent of these efficiency theories is the *Elimination of Double Marginalization* ("EDM"). As discussed, vertical mergers occur between companies along the same supply chain, so in a vertical merger context, there are always a minimum of two links: a supplier and a reseller who purchases an input from the supplier.[162] The supplier sets a price

156 *Id.* at 762.
157 *See* United States v. AT&T, Inc., 310 F. Supp. 3d 161, 193 (D.D.C. 2018), *aff'd*, 916 F.3d 1029 (D.C. Cir. 2019) ("Further complicating the Government's challenge is the recognition among academics, courts, and antitrust enforcement authorities alike that 'many vertical mergers create vertical integration efficiencies between purchasers and sellers.'") (internal citation omitted).
158 Blair et al., *supra* note 33, at 767.
159 *See generally* Jonathan B. Baker et al., *Five Principles for Vertical Merger Enforcement Policy*, 33 ANTITRUST 12, 15 (2019).
160 *AT&T*, 310 F. Supp. 3d at 194 (internal citation omitted).
161 *See* Blair et al., *supra* note 33, at 773–81 (listing possible merger efficiency types).
162 *Id.* at 768.

above its costs—a markup—so that it can make a profit.[163] When the reseller purchases the supplier's goods, it must pay the markup price, which becomes a part of its own costs when it resells the supplier's goods in its own product.[164] The reseller then applies its own markup so that it too can profit.[165] The result is a double markup.[166]

Consider how the equation changes if the reseller buys the supplier. The reseller will not charge a markup because it is now part of the vertically merged firm.[167] Now, the combined firm only charges a single markup, resulting in lower prices for consumers.[168] This is EDM.[169]

For decades, antitrust regulators have assumed that most, if not all, vertical mergers result in EDM.[170] In *AT&T*, the court discussed EDM, and the DOJ conceded that the merger would result in $352 million in cost savings to AT&T due to EDM.[171] As the court explained:

> Pre-merger, both Turner Broadcasting and AT&T earned margins over cost before their products reached consumers: Turner Broadcasting earned a profit margin when it licensed content to AT&T, and AT&T earned a profit margin when it sold content to consumers. Post-merger, Turner Broadcasting would not earn a profit margin when licensing content to AT&T because the merged entity would eliminate that cost and, according to Professor Shapiro, pass on some of those cost savings to consumers in order to attract additional subscribers.[172]

This example illustrates the important role EDM plays in vertical merger litigation.

However, some have criticized default assumptions about the existence of EDM. The 2020 Vertical Merger Guidelines state that "vertical mergers often benefit consumers through the elimination of double marginalization, which tends to lessen the risks of competitive

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[163] The ability for the firm to apply a markup rests on the assumption that it has monopoly power. Blair et al., *supra* note 33, at 768.
[164] *Id.*
[165] *Id.*
[166] *Id.*
[167] *Id.* at 768–69.
[168] *Id.* at 769.
[169] For a more thorough economic discussion of EDM, see *id.* at 768–73.
[170] John Kwoka & Margaret Slade, *Second Thoughts on Double Marginalization*, 34 ANTITRUST 51, 51 (2020).
[171] United States v. AT&T, Inc., 916 F.3d 1029, 1046 (D.C. Cir. 2019).
[172] *Id.* at 1044.

harm."[173] The guidelines were controversial when published, and the FTC ultimately withdrew its support in 2021.[174] FTC Commissioner Rebecca Kelly Slaughter criticized the guidelines' "over-emphasis on the benefits of vertical mergers" and that "achieving EDM is not guaranteed. Nor are the benefits of EDM always passed along to consumers."[175] Similarly, Commissioner Rohit Chopra echoed those concerns and, citing comments on the guidelines, stated "few, if any, promised efficiencies from mergers in fact materialize."[176] Further, addressing the *AT&T* decision, Commissioner Chopra noted that despite the forecasted EDM benefits to consumers, AT&T began repeatedly raising prices less than one month after the completion of the merger.[177]

Others have criticized this default position for ignoring the assumptions underpinning the economic theory of EDM. First, for a vertical merger to result in EDM, both the supplier and reseller described above must be monopolists because only monopolists can extract "profits"[178] through a markup.[179] In other words, if both firms cannot charge a markup, there is no double margin to eliminate. In reality, most mergers occur between firms with imperfect competition[180] —meaning

[173] U.S. DEP'T OF JUST. & FED. TRADE COMM'N, VERTICAL MERGER GUIDELINES 2 (2020), https://www.ftc.gov/system/files/documents/reports/us-department-justice-federal-trade-commission-vertical-merger-guidelines/vertical_merger_guidelines_6-30-20.pdf [https://perma.cc/2M3J-GMVG].

[174] Press Release, Fed. Trade Comm'n, Federal Trade Commission Withdraws Vertical Merger Guidelines and Commentary (Sep. 15, 2021), https://www.ftc.gov/news-events/news/press-releases/2021/09/federal-trade-commission-withdraws-vertical-merger-guidelines-commentary [https://perma.cc/V8XU-M7M2].

[175] Rebecca Kelly Slaughter, *Dissenting Statement of Commissioner Rebecca Kelly Slaughter: In re FTC-DOJ Vertical Merger Guidelines Commission File No. P810034*, FED. TRADE COMM'N, at 2, 4 (June 30, 2020), https://www.ftc.gov/system/files/documents/public_statements/1577499/vmgslaughterdissent.pdf [https://perma.cc/NUF9-S8LE].

[176] Rohit Chopra, *Dissenting Statement of Commissioner Rohit Chopra: Regarding the Publication of Vertical Merger Guidelines Commission File No. P810034*, FED. TRADE COMM'N, at 7 (June 30, 2020), https://www.ftc.gov/system/files/documents/public_statements/1577503/vmgchopradissent.pdf [https://perma.cc/U762-ZABQ] (internal citation omitted).

[177] *Id.* at 7 n.35.

[178] Economists differentiate between "monopoly" and "accounting" profits. Monopoly profits refer to the extra profit a monopolist extracts when it charges a price for goods above its marginal cost. Economic theory holds that only a monopolist can do this because perfect competition will force a firm to price its goods equal to marginal cost. By contrast, accounting profits refer to the plain meaning definition of profits. For more information see *profit*, BRITANNICA MONEY (Jul. 20, 1998), https://www.britannica.com/money/profit [https://perma.cc/G22Z-59U6].

[179] Kwoka & Slade, *supra* note 170, at 53–54.

[180] *Id.* at 54.

the firms may possess some market power over prices but fall short of outright monopoly. Ultimately, the extent to which EDM will result with imperfect competition will vary widely depending on economic conditions.[181]

Second, it is possible to achieve EDM cost reductions without a merger through contract.[182] Unintegrated firms can achieve some or all the cost savings of EDM through maximum resale price agreements, sales quotas where the reseller agrees to buy a set minimum quantity in exchange for a lower price, or a two-part tariff agreement.[183] If two unintegrated firms have already engaged in this type of contracting, then logically EDM cannot result from a merger because they have already achieved cost savings. Some have argued that the absence of this type of contracting implies EDM benefits are not present between the firms because if they were, they would have contracted.[184] However, this assertion may not reflect the economic realities of asymmetric information and contracting costs.[185] In other words, unintegrated firms may not realize that they can achieve these efficiencies through contract or practical considerations hinder an agreement's execution. Regardless, the existence of these agreements may nullify the procompetitive effects of the merger in whole or in part.

Third, even if two firms can capture EDM through a merger, it may not result in lower prices for consumers and under certain circumstances, could increase prices. When a vertical merger occurs between companies that produce multiple products, the integrated company may raise the prices of products unaffected by the merger to induce sales of its newly more profitable low-cost product.[186] After a company vertically integrates, EDM reduces the costs of the affected products, allowing for a price reduction.[187] The resulting integrated product can sell for a lower price but will also be more profitable at that price.[188] Accordingly, the company will want to divert sales to its more

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181 *Id.*; Blair et al., *supra* note 33, at 819.

182 Salop, *supra* note 14, at 1971.

183 Blair et al., *supra* note 33, at 782–83.

184 *See* Baker et al., *supra* note 159, at 15 ("If in advance of the merger the parties never considered contracting to eliminate double marginalization, that fact may suggest that EDM would not achieve substantial benefits.").

185 Blair et al., *supra* note 33, at 784.

186 Fernando Luco & Guillermo Marshall, *The Competitive Impact of Vertical Integration by Multiproduct Firms*, 110 AM. ECON. REV. 2041, 2042–43 (2020); *see also* Margaret E. Slade, *Vertical Mergers: A Survey of Ex Post Evidence and Ex Ante Evaluation Methods*, 58 REV. INDUST. ORG. 493, 497, 497 n.7 (2021).

187 Luco & Marshal, *supra* note 186, at 2042.

188 *Id.*

profitable product.[189] If the firm raises the price of its less profitable, unintegrated products, consumers will substitute away from those products and instead purchase the integrated product.[190] This is exactly what occurred when Coke and Pepsi purchased their bottlers. The prices of Coke and Pepsi fell, but the prices of Dr. Pepper products rose where it still used Coke and Pepsi's newly acquired bottlers.[191] The result may have had an anticompetitive effect on pricing.[192] Given most vertical mergers occur between companies with multiple products, particularly in the technology industry, this phenomenon is an important consideration for EDM analysis.[193]

Finally, vertical mergers may not result in EDM for a host of other reasons.[194] EDM is far from guaranteed, and future litigants should expect the need to quantify and prove EDM for a specific transaction.

2. Anticompetitive Effects

While procompetitive theories focus on how mergers create cost efficiencies that benefit consumers, anticompetitive effects attempt to explain under what circumstances the opposite may occur. The anticompetitive theories of harm generated by vertical mergers include *raising rivals' costs* ("RRC"), *foreclosure*, and *two-level entry* (heightened barriers to entry).[195]

The RRC theory of harm posits that a merged firm may raise the prices of its newly acquired company's products thereby raising the costs of rivals who formerly purchased from the acquired firm before the merger.[196] A merged firm would pursue such a strategy because driving up a competitor's costs creates a strategic advantage and may force a rival's

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[189] *Id.*
[190] *Id.*
[191] *Id.*
[192] *Id.* at 2043.
[193] Slade, *supra* note 186, at 497.
[194] *See generally* Kwoka & Slade, *supra* note 170 (detailing instances where EDM will not result).
[195] Blair et al., *supra* note 33, at 785–92. Blair et al. also defines a fourth anticompetitive harm—Misuse of Competitively Sensitive Information (data as a weapon). Given Microsoft's other businesses in cloud computing, internet search, and AI, it may be in a position to use consumer data related to gaming anticompetitively. *See* Olivia Pakula, Comment, *The Streaming Wars+: An Analysis of Anticompetitive Business Practices in Streaming Business*, 28 UCLA ENT. L. REV. 147, 168–169 (explaining how TV streaming companies use consumer data to their advantage). However, this Article focuses on the effects of RRC, foreclosure, and entry barriers because the FTC's complaint focuses on those harms. *FTC Complaint*, *supra* note 39, at 17.
[196] Blair et al., *supra* note 33, at 785.

exit from the market altogether.[197] RRC can also increase profitability when the integrated firm can raise the market price at current levels of output by more than the firm raises its average costs.[198]

As with EDM, the court in *AT&T* considered, but was ultimately unpersuaded by the DOJ's RRC arguments.[199] The DOJ argued that Turner's bargaining leverage would increase significantly due to its association with AT&T, which would allow it to raise the prices of its video content to rival cable providers, thereby leading to higher-priced cable packages for consumers.[200] It explained that due to the merger, Turner would have less to fear from a "blackout"—a term used to describe a video programmer's removal of its content from the TV provider when the parties failed to reach a new agreement before the existing one lapsed.[201] Under pre-merger circumstances, blackouts led to "catastrophic" losses in advertising and affiliate fee revenues for video programmers, so they face a tremendous incentive to avoid them.[202] However, as the DOJ contended, AT&T could actually use a blackout to drive customers of rival TV providers towards its own TV products, which would retain Turner's channels.[203] While AT&T would still lose some revenue from a blackout, the offset from new customers towards its own services would decrease the harm from a blackout.[204] Ultimately, this offset would change AT&T's bargaining incentives and allow it to negotiate higher prices for Turner's content with rival providers.[205] The DOJ's expert witness, Carl Shapiro, estimated this new dynamic could cost consumers \$286.5–\$561 million per year.[206] However, the court rejected this RRC argument finding there were insufficient facts to support that AT&T would actually obtain increased bargaining leverage.[207]

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197 Steven C. Salop & David T. Scheffman, *Raising Rivals Costs*, 73 AM. ECON. REV. 267, 267 (1983).
198 David T. Scheffman & Richard T. Higgins, *Twenty Years of Raising Rivals' Costs: History, Assessment, and Future*, 12 GEO. MASON. L. REV. 371, 376 (2004).
199 United States v. AT&T, Inc., 310 F. Supp. 3d 161, 164 (D.D.C. 2018), *aff'd*, 916 F.3d 1029 (D.C. Cir. 2019) ("The Government claims, in essence, that permitting AT & T to acquire Time Warner is likely to substantially lessen competition in the video programming and distribution market nationwide by enabling AT & T to use Time Warner's 'must have' television content to . . . raise its rivals' video programming costs . . . .").
200 *Id.* at 201.
201 *Id.* at 200.
202 *Id.*
203 *Id.* at 201.
204 *Id.*
205 *Id.*
206 *Id.* at 225.
207 *Id.* at 200.

RRC has encountered fierce skepticism from some economists who argue it is not supported by economic theory. Economists such as Oliver Hart and Jean Tirole directly challenged Steven Salop, an originator of RRC,[208] and his co-authors, arguing that theory predicted vertically integrated firms would not pursue such cost-raising strategies because market dynamics would force them to compete on price.[209] Another economist Timothy Brennan argued that "RRC's focus on harm to competitors through vertical practices invites analysis of the wrong markets, misapplication of anticompetitive conduct 'tests,' and the revival of antitrust doctrines that condemned welfare-enhancing practices."[210]

Yet, these criticisms may depart from reality. A 2011 study found that vertically integrated firms are more likely to charge higher prices than their unintegrated competitors.[211] It further reported that markets containing vertically integrated firms typically charged higher prices than markets with no vertical integration present.[212] These results suggest RRC is more prevalent than its critics would predict. As Salop and his coauthors quipped in response to Hart and Tirole, "[t]he notion that vertically integrated firms behave differently from nonintegrated ones in supplying inputs to downstream rivals would strike a business person, if not an economist, as common sense."[213] Regardless, RRC has seen widespread recognition among global antitrust regulators.[214]

Ultimately, RRC is not on its own anticompetitive because the net competitive effects may be positive and benefit consumers.[215] It is also difficult to distinguish RRC from legitimate competition.[216] Accordingly, RRC and EDM have been characterized as "two sides of the same coin" that should be analyzed concurrently to understand the net competitive effects of a merger.[217] Recent research suggests that the incentives firms

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[208] Blair et al., *supra* note 33, 785–86; *see also* Salop & Scheffman, *supra* note 197.
[209] Hans Theo Normann, *Vertical Mergers, Foreclosure and Raising Rival's Costs – Experimental Evidence*, 59 J. INDUS. ORG. 506, 508 (2011); *see generally* Oliver Hart & Jean Tirole, *Vertical Integration and Market Foreclosure*, 1990 BROOKINGS PAPERS ON ECON. ACTIVITY: MICROECONOMICS 205 (seminal article challenging RRC theories).
[210] Timothy J. Brennan, *Understanding "Raising Rivals' Costs"*, 33 ANTITRUST BULL. 95, 96 (1988).
[211] Normann, *supra* note 209, at 524.
[212] *Id.* at 518.
[213] Janusz A. Ordover et al., *Equilibrium Vertical Foreclosure: Reply*, 82 AM. ECON. REV. 698, 698 (1992).
[214] Joshua D. Wright, *Moving Beyond Naïve Foreclosure Analysis*, 19 GEO. MASON L. Rev. 1163, 1163 (2012).
[215] II David T. Scheffman & Richard S. Higgins, *Raising Rival's Costs*, *in* THE OXFORD HANDBOOK OF INTERNATIONAL ANTITRUST ECONOMICS 65–66 (D. Daniel Sokol & Roger D. Blair eds., 2014).
[216] *Id.* at 66.
[217] Blair et al., *supra* note 33, at 762, 765, 816.

face to engage in RRC depend on the size of EDM.[218] Price decreases stemming from EDM affect the demand for both the integrated firm's products and its rival's products (because consumers will migrate from the relatively high prices of the rival's products to the lower ones of the integrated firm).[219] The higher the margins pre-merger, the more potential that exists for large drops in prices and consequent shifts in demand.[220] Therefore, large EDM effects may lead to significant RRC incentives.[221] Determining which one is larger depends on a variety of factors such as the slope of the firm's demand curve and relative bargaining strength.[222] The prevailing economic consensus holds that the benefits of EDM will usually exceed RRC.[223]

In actual vertical merger analysis, EDM and RRC theories result in a battle of economic models.[224] For example, in *AT&T*, the parties disputed the true extent of the reduction in cost AT&T would enjoy after acquiring Turner Broadcasting.[225] The DOJ relied on Carl Shapiro's economic model, which predicted that AT&T's ability to raise prices on rivals would far exceed its own cost savings, resulting in net harm to consumers.[226] AT&T countered this model with analysis from Dennis Carlton who argued that past vertical mergers in the same market had not resulted in higher prices for consumers.[227]

Similarly, complete foreclosure occurs when the newly combined firm denies access to the acquired firm's products to rivals.[228] Foreclosure is closely related to RRC, and many scholars characterize it as a special case or extreme version.[229] Accordingly, one anticompetitive risk of foreclosure is that it can lead to RRC.[230] However, foreclosure does not

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218 Gopal Das Varma & Martino De Stefano, *Equilibrium Analysis of Vertical Mergers*, 65 ANTITRUST BULL. 445, 446 (2020).
219 *Id.*
220 *Id.*
221 Blair et al., *supra* note 33, at 793.
222 Slade, *supra* note 186, at 506.
223 Blair et al., *supra* note 33, at 762.
224 Discussions of EDM and RRC were absent from the Northern District of California's recent decision on the Microsoft-Activision merger. Although the opinion does discuss efficiencies and foreclosure. *See generally* FTC v. Microsoft Corp., No. 23-cv-02880-JSC, 2023 WL 4443412, at *1 (N.D. Cal. Jul. 10, 2023).
225 United States v. AT&T, Inc., 916 F.3d 1029, 1036 (D.C. Cir. 2019).
226 *Id.*
227 *Id.*
228 Carl Shapiro, *Testing Vertical Mergers for Input Foreclosure*, ORG. FOR ECON. COOP. & DEV., at 3 (Sep. 17, 2020), https://one.oecd.org/document/DAF/COMP/WD(2019)75/en/pdf [https://perma.cc/WKW6-CGRT].
229 Blair et al., *supra* note 33, at 765.
230 Wright, *supra* note 214, at 1166.

automatically imply an RRC effect and must be quantitatively proven.[231] As a more extreme form of RRC, foreclosure creates an added risk that by excluding rivals from access to an input, it may prevent rivals from maintaining the minimum scale required to stay in business.[232] In other words, foreclosure can harm competition by increasing entry barriers.[233] This has obvious implications for video games: if one console maker controls a high enough proportion of all games and excludes those games from rivals, then it would preclude rival console makers from obtaining a minimally necessary portfolio of games for a successful console.[234]

Antitrust scholars and economists most commonly minimize the risk of foreclosure by arguing that firms will rarely have an incentive to foreclose rivals from their products.[235] The underlying logic is intuitive: if a firm withholds products from rivals, it foregoes revenue and will lose profits.[236] Studies on vertical integration confirm this logic, finding that foreclosure rarely occurs post-merger.[237] However, while this logic may apply in many conventional markets, it ignores how network effects alter firm incentives in two-sided markets. Accordingly, the next Part discusses platform economics and how the Agencies should evaluate vertical mergers of platforms.

IV. PLATFORMS—ECONOMICS AND ANTITRUST

The previous Part discussed vertical merger law generally and how it applies in a traditional antitrust setting. However, video games belong to a special class of firms called platforms. While the overall analysis of a vertical merger involving a platform need not change, an acquisition involving a platform may make anticompetitive outcomes more likely. This Part describes the characteristics of platforms and how they respond to unique economic incentives. Next, this Part discusses how the presence of a platform may alter the antitrust analysis of vertical mergers.

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231 Blair et al., *supra* note 33, at 789–90.
232 Wright, *supra* note 214, at 1166, 1168.
233 Khan, *supra* note 102, at 1008.
234 *See* Evans, *supra* note 32, at 371 (explaining foreclosure is a problem when "one firm has exclusivity over most or all of the market and if the exclusivity is persistent and durable").
235 Wright, *supra* note 214, at 1168.
236 Blair et al., *supra* note 33, at 788 ("[A]s a general matter, vertical integration does not incentivize a firm to eliminate sales to or purchases from unintegrated firms. Profit-maximizing firms, regardless of whether they are vertically integrated, will sell to unintegrated rivals if the price paid by those rivals exceeds marginal cost and will purchase inputs from unintegrated rivals if the cost is lower than that of alternatives, including self-supply.").
237 *Id.* at 789.

Understanding the nexus between platforms and vertical merger law is important because virtually all Big Tech firms operate platforms, and their conduct is the subject of much political and regulatory scrutiny.[238]

A. *Platform Basics and Video Games as Platforms*

Platforms pervade the modern economy. Today's consumers interact with platforms on a daily basis, including products from companies such as Amazon, Uber, and Apple. Platforms are characterized by "two-sided commerce."[239] In other words, the product's value depends on two distinct groups of users coming together to transact on the platform.[240]

For example, Uber is a platform because it requires both drivers and riders. Without drivers, riders derive no value from the app (the platform) and vice versa.[241] Video game consoles are another example of platforms. If a consumer buys a console for which there are no games, then he or she will have nothing to play. Likewise, a game is useless without gamers and a console to play it on. Scholars often use video games as the "canonical example of a multisided platform market" and are the most studied industry within academic literature on platform competition.[242]

Platforms are plagued by what is dubbed the *chicken-and-egg* problem, meaning neither side will participate in the platform without existing participation from the other side.[243] In the context of video games, this means that developers will not create games for a console without gamers who have purchased it, but gamers will not buy a console if they are no games to play. Consequently, the more users that participate on either side, the more valuable the platform becomes to the other. Economists refer to this as *indirect network effects*.[244] In video games, developers value the console the more consumers purchase it, and consumers value their console the more games that are available to play.[245]

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[238] *See supra* Part I.
[239] Hovenkamp, *supra* note 28, at 720.
[240] *Id.* at 715.
[241] *Id.* at 720.
[242] Joost Rietveld & Melissa A. Schilling, *Platform Competition: A Systematic and Interdisciplinary Review of the Literature*, 47 J. MGMT. 1528, 1534 (2020) (surveying interdisciplinary literature on platform competition from 1985–2019); *see also*, *e.g.*, Hovenkamp, *supra* note 28, at 723, 725, 727, 735 (using video games as an example of platforms throughout).
[243] Hovenkamp, *supra* note 28, at 720.
[244] Evans, *supra* note 32, at 332.
[245] *Id.* at 332.

Over time, network effects accumulate and can further entrench a platform's dominance.[246]

Platforms also compete with other platforms. Uber must compete with Lyft, just as Xbox must compete with PlayStation. *Multi-homing* refers to users on either side that use two or more competing platforms.[247] Video game studios engage in multi-homing when they create a game for both Xbox and PlayStation.[248] However, they may choose to *single-home* by developing games for only one console.[249] Even when users multi-home, they may still prefer one platform over the other.[250] Riders may prefer Lyft over Uber, and gamers who own both a PlayStation and an Xbox may prefer one over the other. The extent to which users multi-home or single-home on one side will typically affect the decision to multi-home or single-home on the other.[251] Most gamers single-home because consoles cost hundreds of dollars.[252] Accordingly, many game studios multi-home by releasing their games across multiple consoles to reach more customers.[253]

To attract users, platforms will often engage in *steering* to induce users from one side to select their platform over another.[254] Ultimately, steering is an attempt to deter multi-homing and is often viewed as procompetitive.[255] For example, Lyft was the first to introduce a driver-tipping feature, which induced more drivers to join the platform.[256] This increased the overall value of the platform and forced Uber to respond with its own feature to compete.[257] Thus, this sort of steering behavior increases competition and innovation.

However, some steering can be anticompetitive. Platforms can engage in *exclusive dealing*, where suppliers agree to offer their products exclusively for one platform.[258] In video games, the benefits are obvious

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[246] Steven C. Salop, *Dominant Digital Platforms: Is Antitrust Up to the Task?*, 130 YALE L. J. 563, 571 (2021).
[247] Hovenkamp, s*upra* note 28, at 726.
[248] Lee, *supra* note 41, at 2965.
[249] *Id.*
[250] Hovenkamp, s*upra* note 28, at 726.
[251] *Id.* at 726–27.
[252] Although this could be changing as more gamers increasingly own more than one console. Matt Gardner, *Goodbye Console Wars? Dual PlayStation and Xbox Ownership Is Booming*, FORBES (Oct. 15, 2021, 5:30 AM), https://www.forbes.com/sites/mattgardner1/2021/10/15/goodbye-console-wars-dual-playstation-and-xbox-ownership-is-booming/?sh=5f8a35bbc327 [https://perma.cc/SR2H-7QAV].
[253] Hovenkamp, *supra* note 28, at 727.
[254] *Id.*
[255] *Id.*
[256] *Id.*
[257] *Id.*
[258] *Id.* at 730.

because if a popular video game is only available on one console, then consumers will be more likely to choose that console over a competitor.[259] Nascent and established platforms both pursue exclusivity to enhance network effects but do so for different reasons. While nascent platforms need to obtain minimum scale to combat the chicken-and-egg problem, established platforms do so to protect their existing business.[260] Therefore, exclusive dealing is not necessarily anticompetitive because it is an important tool for new entrants.[261] This is particularly true for video games where exclusive game titles were essential to cementing each of the Big 3's consoles as viable platforms.[262] However, exclusivity creates problems when it prevents a competing platform from maintaining the critical mass necessary to survive or barring new entrants, i.e., foreclosure.[263] Once an existing platform obtains enough critical mass, network effects become self-reinforcing and create higher barriers to entry due to switching costs.[264] The very same network effects a dominant platform needed for its own viability become a means to prevent rivals from entering the market.[265] Thus, exclusivity and associated network effects can ensure long-term dominance.[266]

The foregoing discussion illustrates the delicate balance between procompetitive and anticompetitive conduct of platform firms. On the one hand, steering and exclusive dealing are tools fundamental in combating the chicken-and-egg problem and creating any market at all. However, a dominant platform may also abuse these tools by forestalling new competition and stifling innovation.

B. *Analysis of Platform Vertical Mergers*

The preceding Section discussed how platforms differ from conventional markets. How then, if at all, should an acquisition by a platform affect merger review? The ultimate framework of balancing competitive effects need not change, and traditional tools should identify

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259 *See id.* at 730–31 ("[I]n the platform context, the arrangement may generate a reinforcing feedback effect: users on [the buy-side] now deem the platform more attractive due to the fact that many [suppliers] can only be reached on this platform. Thus, many [buy]-side users will now switch to the platform and away from competitors.").
260 Jullien & Sand-Zantman, *supra* note 34, at 24.
261 Lee, *supra* note 41, at 2962.
262 For a more thorough discussion, see *infra* Section V.B.1.
263 Wright, *supra* note 214, at 1166.
264 Khan, *supra* note 102, at 1079 (arguing digital platforms deserve more antitrust scrutiny).
265 *Id.*
266 *Id.*

those effects.[267] However, a platform acquisition may lead to anticompetitive outcomes not ordinarily observed because network effects and economies of scale can increase barriers to entry and further entrench a dominant platform.[268]

EDM and RRC are still fundamental components of a vertical merger involving platforms and should be analyzed in the same way.[269] However, platform firms operate many kinds of business models.[270] For example, a platform like Facebook charges consumers on one side nothing to the use platform but charges advertisers on the other. In contrast, some platforms, like gaming consoles, charge users on both sides of the platform. The strength of network effects relative to the margins obtained premerger can have varying outcomes on consumer surplus post-merger.[271] These diverse business practices only serve to complicate what is already a highly individualized and ambiguous exercise for vertical merger analysis.[272] Thus, there is no general rule on the net competitive effects of platform vertical mergers, and the Agencies must conduct merger-specific inquiries into EDM and RRC.

However, foreclosure may be more likely in platform vertical mergers because exclusive dealing is a common profitability strategy.[273] Contemporary antitrust analysis views foreclosure as an unlikely outcome for conventional markets because such a strategy would likely reduce

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267 *See*, *e.g.*, Katz & Sallet, *supra* note 32, at 2169 ("[T]here is no need to create a specialized doctrine applicable only to multisided platforms. Existing antitrust principles are capable of evaluating the competitive effects of a multisided platform's conduct."); Hovenkamp, *supra* note 28, at 715 ("[Platform] considerations can (and should) be accounted for within the established structure of antitrust's' 'rule of reason' analysis, which is a multi-stage burden shifting framework.").

268 Salop, *supra* note 246, at 563 ("Digital networks are a particular concern because barriers to entry, which result from substantial network effects and economies of scale and scope, rise as platforms' dominance is enhanced.").

269 Jullien & Sand-Zantman, *supra* note 34, at 27–28 ("Vertical integration by platforms may have several efficiency motivations. In particular, as in any vertical supply chain, it may raise volumes by eliminating 'double marginalization'. . . While vertical integration in complementary services by platforms may improve coordination, it also raises the issue of the foreclosure of competing third-party suppliers of complementary services.").

270 *Id.* at 32 ("Some may charge all sides while others charge only one side; some may rely on subscription while others rely on transaction fees.").

271 *Id.* ("When pre-merger margins are large relative to network externalities, all prices increase and consumer surplus declines on both sides. But when all margins are small and total network effects are large, the merger benefits all users due to a reduction of market fragmentation.").

272 *See* Blair et al., *supra* note 33, at 766–67 (describing the difficulty associated with determining net competitive effects of vertical mergers).

273 *See* Evans, *supra* note 32, at 371 ("Another possible difference between multi-sided and one-sided markets is that the potential for profits on the other side provides a possible incentive for exclusive contracts.").

profits.[274] But for platforms, exclusivity might be *the* reason for the acquisition. The more unique features or content a platform can offer, the more consumers will value it compared to a rival platform, increasing adoption.[275] Pursuing greater network effects then provides a profitable basis for exclusive contracting. An acquisition is merely an extreme form of an exclusive contract that guarantees exclusivity in the long term.[276] In particular, media and other creative industries depend on a constant flow of new high-quality content, and an acquisition guarantees that content will appear on the acquirer's platform.[277] Accordingly, the presence of a platform increases the likelihood that a firm will pursue foreclosure post-merger.

V. APPLYING PLATFORM VERTICAL MERGER ANALYSIS TO MICROSOFT-ACTIVISION

Thus far, this Article has described how the law generally applies to vertical mergers and how the presence of a platform may affect anticompetitive outcomes. This Part applies that analysis to the Microsoft-Activision merger and shows how platform incentives can lead to anticompetitive outcomes.[278]

A. *EDM and RRC*

In its complaint, the FTC alleged Microsoft would obtain "total control over Activision's content, thereby giving Microsoft the ability to . . . raise rivals' costs."[279] In response, Microsoft asserted that the acquisition "will be procompetitive" and "result in substantial acquisition-specific efficiencies, synergies, and other procompetitive effects that will directly benefit consumers."[280] The pleadings confirm that an analysis of the net

[274] *See supra* Section III.C.2.
[275] Hovenkamp, *supra* note 28, at 731.
[276] Herbert Hovenkamp, *The Law of Vertical Integration and the Business Firm: 1880–1960*, 95 IOWA L. REV. 863, 883, 909 (2010) ("[W]e tend to see the differences between ownership and contract vertical integration as minimal" and "outright vertical integration by ownership is more 'absolute' and generally more durable than integration by contract").
[277] Gil & Warzynski, *supra* note 49, at i144.
[278] This Part analyzes the merger under its original terms before Microsoft restructured it to address the CMA's concerns. *See supra* notes 84–85 and accompanying text. The CMA's concerns towards the original deal cited throughout this Part are still applicable to antitrust concerns in the United States as the deal's restructuring did not affect streaming rights outside of Europe. *See supra* notes 84–85 and accompanying text.
[279] *FTC Complaint*, *supra* note 39, at 18.
[280] *Microsoft Answer*, *supra* note 77, at 32.

competitive effects of RRC and EDM has an important role in vertical merger challenges.

As in *AT&T*, parties need to supply their own economic models and data in support of their competitive effects assertions.[281] Under the *Baker Hughes* framework, the Agencies must first show anticompetitive effects.[282] In *AT&T*, the DOJ primarily relied on the economic model of its expert Carl Shapiro to show RRC.[283] However, the court rejected the DOJ's models finding there were insufficient facts to support that AT&T would actually obtain and act upon increased bargaining leverage.[284]

AT&T also proffered its own economic analysis of prior mergers in the television industry, and to its detriment, the DOJ declined to conduct its own analysis.[285] AT&T's model showed that RRC had not resulted in three prior vertical mergers.[286] Notably, the model showed Comcast's acquisition of NBC—an analogous situation of a provider buying a video programmer—resulted in no statistically significant RRC, and the DOJ had approved that transaction under similar terms.[287] While the DOJ attempted to undermine AT&T's model, it never conducted its own analysis of those related mergers.[288] This case showed the importance of "real-world data" as opposed to projections modeling the merger.[289] Further, the DOJ missed an opportunity to rebut AT&T's analysis with its own. It possibly could have offered a different perspective on the cost-raising implications of that data.

The Agencies should not make the same mistake with other future platform mergers. With many acquisitions in the technology space in recent years, the Agencies should be prepared to provide their own analysis of those transactions. Regarding the subject of this Article, the video game industry has observed many acquisitions in recent years by Sony and Microsoft.[290]

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281 *See* discussion *supra* Section III.C.2.

282 United States v. AT&T, Inc., 310 F. Supp. 3d 161, 194 (D.D.C. 2018), *aff'd,* 916 F.3d 1029 (D.C. Cir. 2019).

283 *Id.* at 201.

284 *Id.*

285 *See id.* at 215–18 (finding the DOJ's arguments discrediting AT&T's model unpersuasive).

286 *Id.* at 215.

287 *Id.* at 215–217.

288 *Id.*

289 *See id.* at 215 (Suggesting AT&T's data on actual mergers in the industry was more "real-world" than the DOJ's self-professed real-world data attempting to predict the transaction's effects); *see also* James A. Keyte, *The AT&T/Time Warner Decision: More than Meets the Eye*, 33 ANTITRUST 20, 24 (2019) ("[T]he court's discussion highlights the importance of 'real-world' data . . . .").

290 *See generally* Alexander, *supra* note 61 (describing recent consolidation in industry); *see also* Liao & Grayson, *supra* note 61 (same).

One such study provides a glimpse of the possible net welfare effects of video game industry vertical mergers. In 2015, Economists Gil and Warzynski[291] studied the effect of video game industry vertical mergers using monthly sales data from 2000–2007.[292] They analyzed how the presence of vertical integration—either independent publishers buying developers or console makers buying developers—affected game prices and quality.[293] They found that games developed with some level of vertical integration sell for higher prices and at higher quantities (and thus higher revenue) than those without integration.[294] This suggests an anticompetitive effect on pricing. However, integrated developers made better games because they could better coordinate development due to improved release strategies and the selection of higher-quality games for development.[295] Overall, these results are ambiguous[296] because consumers pay higher prices for games, but those games are better quality.[297]

Notably, the author's results show an efficiency that leads to higher prices, not lower, for consumers. Gil and Warzynski explain that coordination enabled developers to stagger release dates of games farther apart to soften competition for their own games, increasing sales.[298] This ultimately harms consumers[299] because video games release at a high price and then decrease rapidly.[300] In other words, consumers can only play one game at a time. If two desirable games are simultaneously released, the consumer may only buy one and forego the other until they have finished

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291 Their study has been well-cited in vertical merger literature. *See, e.g.*, Slade, *supra* note 186, at 498; Ted Lipsky et al., *The Federal Trade Commission's Hearings on Competition and Consumer Protection in the 21st Century, Vertical Mergers, Comment of The Global Antitrust Institute, Antonin Scalia Law School, George Mason University* 7–8 (Geo. Mason Univ., Research Paper No. 18-27, 2018), https://papers.ssrn.com/sol3/Delivery.cfm/SSRN_ID3245940_code410506.pdf?abstractid=3245940&mirid=1&type=2 [https://perma.cc/WC84-YMRA].

292 Gil & Warzynski, *supra* note 49, at i145.

293 *Id.* at i145–46.

294 *Id.* at i146.

295 *Id.* at i147.

296 A prominent survey of past vertical mergers suggests Gil & Warzynki's results are net procompetitive. However, the authors do not explain their reasoning. *See* Lipsky et al., *supra* note 291, at 8 tbl.

297 *See* Marissa Beck & Fiona Scott Morton, *Evaluating the Evidence on Vertical Mergers*, 59 REV. INDUS. ORG. 273, 295 (2021) ("Such a regression cannot determine whether the higher prices and volumes indicate consumer harm—e.g., because vertical integration raises rivals' costs and causes consumers to switch away from those games—or consumer benefit: e.g., because vertical integration leads to higher quality games that increase demand.").

298 Gil & Warzynski, *supra* note 49, at i163–64.

299 Beck & Morton, *supra* note 262, at 295 ("[S]taggering release dates to soften competition" is "a form of consumer harm . . . .").

300 Gil & Warzynski, *supra* note 49, at i163.

playing the first, at which point the price likely has decreased.[301] Staggering increases the likelihood that the consumer will pay the higher price at both times.

However, several limitations to this study limit its probative value for a current video game merger challenge. First, the data used in the study is dated. Its most recently examined data is now 16 years old, and the industry has changed substantially since then.[302] Further, the authors did not quantify net competitive effects, and their model cannot differentiate EDM from RRC.[303] Finally, Gil and Warzynski examined acquisitions by both publishers and console-makers and do not differentiate the results.[304] In other words, the analysis focused on the effect any merger had on game prices, regardless of whether the acquirer was a publisher or a console maker.[305] Moreover, console-maker-developed games made up less than 5% of the data.[306] Future analysis should quantify the net competitive effects of recent console-maker acquisitions.

Finally, the Agencies should be wary of introducing their own EDM estimates. While the court in *AT&T* rejected the DOJ's RRC theory of harm, it was happy to accept the agency's EDM numbers.[307] Instead, the Agencies should force acquirers to prove EDM as an affirmative defense, as the DOJ has advocated.[308] For the reasons discussed

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301 *See* Gil & Warzynski, *supra* note 49, at i164 ("[P]ublishers soften competition at release for internally developed games more than they do for independently developed games hoping to increase sales for their own vertically integrated games.").

302 From 2000–2007, the prominent consoles were Sony's PlayStation 2, Nintendo's GameCube, and Microsoft's original Xbox. The end of this period barely captures the introduction of the next generation of consoles—the PlayStation 3, Wii, and Xbox 360. *Id.* at i147. Since then, each of the Big 3 have launched another generation, and all are moving towards streaming in the next. *See* discussion *supra* Part II.

303 Beck & Morton, *supra* note 297, at 295.

304 *See* Gil & Warzynski, *supra* note 49, at i145 ("Our analysis differs from the existing platform literature in that we focus on the game as unit of analysis and more precisely the impact of the contractual relationships between developers and publishers on game performance. Existing studies have mainly focused on vertical integration between publishers and platforms while proxying vertical integration with software exclusivity.").

305 *Id.* ("We focus our analysis in a sample of 3026 games (out of a total of 3365) containing [console-maker] developed [games] and independent games published by integrated publishers.").

306 *Id.* at i154.

307 *See* United States v. AT&T, Inc., 310 F. Supp. 3d 161, *passim* (D.D.C. 2018), *aff'd*, 916 F.3d 1029 (D.C. Cir. 2019) (referring repeatedly to "the conceded $350 million in annual cost savings to AT & T's customers").

308 Former Assistant Attorney General Makan Delrahim has stated that EDM is no different than any other affirmative defense where the defendant bears the burden of proof. Symposium, *"Harder, Better, Faster, Stronger": Evaluating EDM as a Defense in Vertical Mergers*, 26 GEO. MASON L. REV. 1427, 1431 (2019). He further stated that an EDM

previously, the video game industry may be subject to market conditions where EDM will not result post-merger.[309] As explained in the next Section, the Big 3 routinely secure exclusive titles through contract.[310] This may suggest that the parties have already captured cost efficiencies through those agreements.[311] Further, Microsoft is a multiproduct firm where further vertical integration could actually result in higher prices.[312] Given the incentives common to all platforms, these same pre-merger market conditions that could prevent EDM would likely also be present in other platform vertical mergers.

The FTC has repeated some of the DOJ's mistakes fighting the Microsoft-Activision merger, and its model suffered a similar fate as in *AT&T*. In its request for a preliminary injunction against the merger, the FTC relied on a foreclosure theory,[313] arguing that Microsoft had the ability and incentive to withhold *Call of Duty* from competitors.[314] The FTC's expert, economist Robin Lee, estimated that making *Call of Duty* exclusive would increase Xbox's share of the console market by 5.5 percent.[315] Among other problems with the assumptions underpinning the model, the court found it suffered from evidentiary failures.[316] The model's assumptions lacked support, and it could not overcome real-world evidence showing that Microsoft had no economic incentive to withhold *Call of Duty*.[317] Namely, the court highlighted Microsoft's sworn commitments to keep *Call of Duty* on rival platforms, evidence of reputational harm from making the game exclusive, lack of showing corporate documents indicating an exclusivity strategy, and the benefits of cross-platform play to users.[318]

Similarly, the FTC failed to effectively counter Microsoft's expert Dennis Carlton. Carlton, also AT&T's expert, challenged Lee's model and

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defense has three evidentiary requirements: (1) pre-merger market conditions existed that allowed both firms to impose a markup; (2) the firms did not eliminate those markups through contract; and (3) the extent to which EDM would result in lower prices for consumers. *Id.* These requirements track closely to the theoretical assumptions underpinning EDM discussed in Section III.C.1.

309 *See* discussion *supra* Section III.C.1.

310 *See* discussion *infra* Section V.B.1.

311 *See* discussion *supra* Section III.C.1.

312 *See* discussion *supra* Section III.C.1.

313 Foreclosure is discussed in more detail in *infra* Section V.B. But as this Section focuses on evidentiary failures supporting models, the Article discusses it briefly here.

314 FTC v. Microsoft Corp., No. 23-cv-02880-JSC, 2023 WL 4443412, at *12 (N.D. Cal. Jul. 10, 2023).

315 *Id.* at *16.

316 *See id.* at *16–17.

317 *Id.*

318 *Id.* at *13–14, *17.

provided testimony supporting Microsoft's position on *Call of Duty*.[319] The FTC did nothing to challenge Carlton's testimony.[320] Carlton further provided evidence of procompetitive effects of adding *Call of Duty* to Xbox's Game Pass subscription.[321] Again, the FTC offered no evidence of how exclusive Activision content on Game Pass could harm competitors.[322]

Whether the FTC provided modeling on prior video game industry mergers is unclear.[323] The court's analysis largely focused on whether Microsoft had any incentive at all to foreclose Activision content.[324] Thus, the court had little reason to proceed on to examine anticompetitive effects.[325] Regardless, a new study of recent mergers, like that of Gil's & Warzynski's, could have helped show RRC and an incentive to engage in that conduct.

Further, it is unclear how, if at all, Microsoft quantified procompetitive effects. The court discussed Carlton's testimony that adding *Call of Duty* to Game Pass would reduce consumer costs and expand consumer access to the game, but it does not mention any of the modeling underpinning those assertions.[326]

The FTC's loss to Microsoft on the preliminary injunction again underscores the importance of effective modeling and real-world data to support its assumption. Like the DOJ, the FTC missed opportunities to bolster its own model and challenge the assumptions of its opponent.

B. *Foreclosure*

Complete foreclosure and exclusivity are closely related concepts, and platforms may have a greater incentive to foreclose rivals post-merger due to network effects.[327] Courts accept that in certain circumstances, exclusivity can harm consumers through higher prices by foreclosing

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319 *Id.* at *17.

320 *Id.* ("And what does Prof. Lee say about Dr. Carlton's criticism? Nothing in his direct testimony. At the evidentiary hearing on re-direct? Nothing. And when the FTC cross-examined Dr. Carlton on his written direct testimony? Again, nothing. The FTC chose not to challenge, or even address, Dr. Carlton's identification of material flaws in Prof. Lee's share model. The criticism thus stands unscathed—and persuasive.") (cleaned up).

321 *Id.* at *19.

322 *Id.*

323 Lee's model seems to have focused on the incentive to make games exclusive rather than the effect mergers can have on competition. *See id.* at *16 (discussing Lee's model).

324 *Id.* at *passim*.

325 *See id.* at *12 ("If there is no incentive to foreclose, then there is no probability of foreclosure and the alleged concomitant anticompetitive effect.").

326 *Id.* at *19.

327 *See* discussion *supra* Section IV.B.

supply to existing rivals or preventing new entrants.[328] In vertical mergers, the Agencies search for the ability and incentive of the combined firm to exclude products from competitors, thereby foreclosing their ability to compete at all or creating entry barriers for new firms.[329] Excluding products may mean completely withholding the product or only supplying an inferior form (degradation).[330] Accordingly, whether Microsoft or any other platform would foreclose content turns on whether it has the ability and incentive to do so.

The FTC alleged that by assuming total control over Activision's content, Microsoft would have the ability and incentive to withhold Activision's games from rivals or employ several strategies to degrade them.[331] To evaluate Microsoft's ability and incentive to foreclose, this Section first explores the long-standing practice of the Big 3 to engage in exclusive dealing. This history shows that exclusive games have been an indispensable strategy in the video game industry and will continue to be. Accordingly, the proper question is not whether Microsoft will withhold Activision's content, but to what extent? The video game industry's history of exclusive dealing illustrates how platforms generally benefit from exclusivity. Next, this Section discusses Microsoft's specific ability and incentive to foreclose rivals. Then, it shows how foreclosure could harm consumers and competition in the video game industry. This analysis provides an example of how platform foreclosure can result in anticompetitive harm.

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[328] *See* U.S. Healthcare, Inc. v. Healthsource, Inc., 986 F.2d 589, 595 (1st Cir. 1993) ("[A]n exclusive arrangement may 'foreclose' so much of the available supply or outlet capacity that existing competitors or new entrants may be limited or excluded and, under certain circumstances, this may reinforce market power and raise prices for consumers.").

[329] Steven C. Salop, *The 2020 Vertical Merger Guidelines: A Suggested Revision (Version: April 30, 2022)*, 67 ANTITRUST BULL. 371, 376 (2022) ("A vertical merger may diminish competition by giving the merged firm the ability and incentive to weaken or remove the competitive constraint of one or more of its actual or potential rivals in the relevant market by changing the terms of those rivals' access to one or more related products. . . . [F]oreclosure can involve the merged firm totally withholding access to its input, . . . or otherwise disadvantaging rivals by worsening their access to the inputs produced by the upstream merging firm. . . . The fear of input foreclosure also may raise entry barriers.").

[330] *Id.*

[331] *FTC Complaint*, *supra* note 39, at 18–19 (Degradation strategies include "timed exclusivity, exclusive downloadable content available only on Microsoft's products, and a variety of other means . . . degrade the quality of Activision content on competing consoles and subscription services and create a less desirable player experience for users choosing to play anywhere other than on Microsoft's products . . . reduce efforts to optimize Activision content for rival products. Currently, Activision collaborates closely with gaming hardware manufacturers to ensure an optimal experience for gamers." It has an incentive to do this because withholding or degrading Activision's content would allow it to "gain significant profits from additional gamers purchasing Xbox consoles or Xbox Game Pass.").

1. Historical Exclusivity in Video Games

Platform exclusivity is nothing new in the video game world. Household names such as *Super Mario Bros.*, *Pokémon*, and *The Legend of Zelda* have long been Nintendo's exclusive IP.[332] Since the launch of the original PlayStation, Sony has released games such as *Crash Bandicoot*, *Spider-Man*, and *God of War* as PlayStation exclusives.[333] When Microsoft entered the video game market in 2001, gamers could only play the instant hit *Halo* on the Xbox, cementing its viability as a console in an already fiercely competitive market.[334] From the years 2000–2005, over 60% of all games were exclusive to one console.[335]

At the outset of creating a video game, studios face a choice: offer their game exclusively for one console (single-homing) or multiple platforms (multi-homing).[336] By multi-homing, studios may obtain higher sales because their game will be more accessible to more users.[337] However, studios may opt to single-home because developing a video game for more than one console requires more investment.[338] Referred to as *porting costs*, the investment required to develop a game for multiple consoles ranges from hundreds of thousands to millions of dollars.[339] To steer developers towards single-homing, console makers often offer large monetary incentives to make up for the possible shortfall in revenue. For example, Microsoft reportedly paid Take-Two, a publisher, approximately $50 million to make *Grand Theft Auto IV: The Lost and Damned* exclusive

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332 *See Nintendo Console*, BRITANNICA (Feb. 7, 2023), https://www.britannica.com/technology/Nintendo-console [https://perma.cc/32J7-65ZN] (describing *Super Mario Bros.* and *The Legend of Zelda* as Nintendo games dating back to the 1980s); *Pokémon*, BRITANNICA (Oct. 16, 2023), https://www.britannica.com/topic/Pokemon-electronic-game [https://perma.cc/PUK8-YWVQ] (describing *Pokémon* as a Nintendo game that launched in 1996).

333 *The Best PlayStation Exclusives of All Time*, IGN (Apr. 22, 2022), https://www.ign.com/articles/best-playstation-exclusives [https://perma.cc/J3AU-9R99].

334 Marc Graser, *The 'Halo' Effect*, 420 VARIETY, Sep. 6, 2010, at 1; *see also* Leo Sun, *Why 'Halo: The Master Chief Collection' Will Save the Xbox One*, MOTLEY FOOL (July 1, 2014, 7:36 AM), https://www.fool.com/investing/general/2014/07/01/why-halo-the-master-chief-collection-will-save-the.aspx [https://perma.cc/TY8V-94MZ] ("If Bungie Studios hadn't created [Halo], the original Xbox might not even have survived long enough to evolve into the Xbox 360.").

335 Lee, *supra* note 41, at 2961.

336 *Id.* at 2965.

337 *Id.*

338 *Id.*

339 *Id.*

for the Xbox 360.[340] Exclusive game titles make a console more valuable, by enhancing network effects and leading to greater profitability.[341]

Exclusivity has been essential for new consoles to enter the market. When Nintendo entered the console market with its Nintendo Entertainment Systems ("NES") in 1985, it used exclusivity to beat out incumbents Atari and Sega.[342] In exchange for the right to develop games for the NES, Nintendo forced all developers to create games exclusively for their system for two years.[343] By 1990, Nintendo claimed 80% of the console market, and Atari eventually filed an antitrust and copyright suit.[344] While Atari ultimately lost, Nintendo only abandoned its forced exclusivity contracts after the FTC opened an antitrust investigation.[345] Instead of forced exclusivity contracts, console makers now induce exclusivity with game studios through favorable contractual terms such as lump sum payments like that paid to Take-Two for *Grand Theft Auto*.[346] Similarly, Sony usurped Nintendo as the console leader in the 1990s aided in large part by convincing game studio Square to make games exclusively for PlayStation.[347] Likewise, Microsoft launched the original Xbox in 2001, and *Halo* helped cement its viability as a console. Empirical evidence also confirms that exclusivity has aided new entrants. A 2013 study found that prohibiting exclusive contracts in the early 2000s would have benefitted existing platforms and stifled new entrants (Xbox).[348]

The foregoing discussion highlights the importance exclusivity has in solving a platform's chicken-and-egg problem. However, the same three console makers have dominated the video game industry for more than two decades.[349] Why then have the Big 3 continued pursuing exclusive game titles and why have they increasingly done so through acquisitions? The reason largely comes down to network effects associated with high-quality exclusive content.[350] Preventing multi-homing on the game studio

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340 Vardit Landsman & Stefan Stremersch, *Multihoming in Two-Sided Markets: An Empirical Inquiry in the Video Game Console Industry*, 75 J. MKTG. 39, 40 (2011).
341 *See* discussion *supra* Section IV.B.
342 Carl Shapiro, *Exclusivity in Network Industries*, 7 GEO. MASON L. REV. 673, 675–76 (1999).
343 Lee, *supra* note 41, at 2965.
344 Atari Games Corp. v. Nintendo of America, Inc., 897 F.2d 1572, 1574 (Fed. Cir. 1990).
345 Lee, *supra* note 41, at 2965.
346 *Id.*
347 Song et al., *supra* note 50, at 102.
348 Lee, *supra* note 41, at 2962.
349 And to a large extent only Sony and Microsoft compete for high-performance titles. *See* discussion *supra* Section II.A.
350 *See* discussion *supra* Section IV.B.

side of the platform raises profits on the consumer side.[351] This is particularly true in the video game industry where a small proportion of extremely popular games drive most console sales.[352] This "superstar" effect is a common phenomenon in platforms.[353] The presence of a superstar helps other supply-side platform participants because more adoption of the platform expands the number of potential customers for other suppliers as well.[354] Superstars are also referred to as "killer apps," and in video game parlance, such games are AAA games. [355] A single AAA games can influence console sales by more than 5 percent.[356] Thus, exclusivity has been a significantly profitable strategy for console makers.

A console maker would pursue an acquisition strategy over an exclusive contract to guarantee future access. The existence of AAA games makes a developer an attractive acquisition target for console makers so that they can secure exclusive access to future installments of a popular game franchise.[357] An exclusive contract may accomplish a platform's exclusivity goals in the short term, but an acquisition guarantees it.

2. Microsoft Would Likely Pursue a Foreclosure Strategy with Activision Content

The preceding Section discussed the inherent profit incentive of console makers to pursue exclusive game titles. This Section examines Microsoft's ability and incentive to do so with Activision content and concludes Microsoft would likely make Activision games exclusive to its platform.

Microsoft will likely exclude rivals from Activision games because it has pursued this strategy with its other mergers. The FTC has noted that Microsoft has pursued exclusivity in its past 10 gaming acquisitions.[358] Notably, Microsoft completed its $7.5 billion acquisition of ZeniMax in

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351 *See* discussion *supra* Section IV.B; *see also* Jullien & Sand-Zantman, *supra* note 34, at 23 ("Preventing multi-homing is unilaterally profitable because multi-homing on one side of the market reduces the revenue that a platform can obtain on the other side of the market.").

352 Song et al., *supra* note 50, at 101.

353 *See* Jullien & Sand-Zantman, *supra* note 34, at 23–24 (describing "superstar" effect).

354 *See id.*

355 Song et al., *supra* note 50, at 101.

356 Lee estimates that without *Halo* as an exclusive game, total Xbox sales would have decreased by as much as 5.5%, equivalent to roughly 700,000 units. Lee, *supra* note 41, at 2969, 2986.

357 Gil & Warzynski, *supra* note 49, at i163.

358 *FTC Complaint*, *supra* note 39, at 3.

2021,[359] and convinced European Regulators it would not foreclose rivals.[360] Shortly thereafter, Microsoft announced ZeniMax's most anticipated upcoming games would be Xbox exclusive.[361] Microsoft's Xbox head, Phil Spencer, admitted that the ZeniMax acquisition was "about delivering great *exclusive* games for [Xbox customers] that ship on platforms where Game Pass exists. That's our goal, that's why we're doing this."[362] Microsoft has expressed a clear intention to acquire game studios with the purpose of making their content exclusive.

Microsoft has disputed that its past actions can predict its intentions with Activision, arguing that the ZeniMax acquisition "has no relevance to the current transaction."[363] The company highlights that two games after the transaction closed were released as PlayStation exclusives and that it has continued to provide updated content for games that were already available on other consoles.[364] However, Microsoft has failed to mention that it was obligated to do so under ZeniMax agreements made before the acquisition.[365] The FTC pursued this argument in its preliminary injunction fight against the merger but failed to convince the court Microsoft would make *Call of Duty* exclusive.[366]

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359 Tom Warren, *Microsoft Completes Bethesda Acquisition, Promises Some Xbox and PC Exclusives*, VERGE (Mar. 9, 2021, 8:33 AM), https://www.theverge.com/2021/3/9/22319124/microsoft-bethesda-acquisition-complete-finalized [https://perma.cc/8JHZ-5E4F].

360 *FTC Complaint*, *supra* note 39, at 4; *see also* EUROPEAN COMMISSION: DG COMPETITION, Case M.10001 MICROSOFT / ZENIMAX at 16, 19–20 (May, 3, 2021), https://ec.europa.eu/competition/mergers/cases1/202124/m10001_438_3.pdf [https://perma.cc/EHB6-R4JG] ("While Microsoft could have the technical ability to implement an exclusivity strategy with regard to ZeniMax games vis-à-vis rival consoles, the Commission considers that the combined entity will not have the ability to engage in a successful input foreclosure strategy.").

361 Warren, *supra* note 338.

362 Tom Warren, *Xbox Boss Says Microsoft's Bethesda Deal Was All About Exclusive Games for Game Pass*, VERGE (Mar. 11, 2021, 2:03 PM) (emphasis added), https://www.theverge.com/2021/3/11/22325757/microsoft-xbox-bethesda-acquisition-game-pass-exclusive-games-phil-spencer-comment [https://perma.cc/A9J9-XMF6].

363 *Microsoft Answer*, *supra* note 77, at 6.

364 *Id.*

365 Andy Robinson, *Xbox Says it Will Honour PS5 Exclusivity Agreements for Deathloop and Ghostwire*, VIDEO GAMES CHRON. (Sep. 21, 2020, 5:45 PM), https://www.videogameschronicle.com/news/xbox-says-it-will-honour-ps5-exclusivity-agreements-for-deathloop-and-ghostwire/ [https://perma.cc/F494-STXD].

366 FTC v. Microsoft Corp., No. 23-cv-02880-JSC, 2023 WL 4443412, at *17 (N.D. Cal. Jul. 10, 2023).

Activision's AAA franchise *Call of Duty* has featured prominently in media commentary[367] and official court documentation.[368] The franchise is immensely popular with the latest installment grossing $1 billion in 10 days.[369] However, Activision has more than just *Call of Duty*. The developer is one of only a handful of independent game studios that can consistently produce AAA games due to their enormous cost and time commitment.[370] The FTC and the UK's CMA expressed concerns over exclusive Activision content and in particular *Call of Duty*.[371] In its final assessment of the transaction, the CMA concluded that Microsoft had an incentive to pursue an exclusivity strategy with Activision games because exclusivity is a proven profitability strategy, Microsoft has pursued that strategy in the past, and the outsize profit potential of AAA games like *Call of Duty* would only make the upside of exclusivity that much stronger.[372] Moreover, the CMA explained that the incentive is even stronger for Microsoft's Xbox Game Pass streaming service because for a nascent platform, "success is highly uncertain for new entrants, and there is a greater opportunity (and stronger incentive) for incumbents to engage in foreclosure strategies in a bid to acquire market power."[373] The CMA's conclusion reinforces the network effect incentives of pursuing a foreclosure strategy in platform industries.

To its detriment, the FTC focused solely on *Call of Duty* in its argument requesting a preliminary injunction. As discussed in Section V.A, the FTC primarily pursued a foreclosure argument solely as to *Call of Duty*.[374] The court found persuasive testimony from Microsoft executives that they had no intention of making *Call of Duty* exclusive in the console market.[375] Instead, the FTC should have focused on Activision's entire portfolio of games and AAA development capabilities. The court seemed to lament the fact that the FTC did not provide evidence on other games, noting it "focused on *Call of Duty*, rather than other Activision AAA

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367 *See, e.g.*, *Microsoft, Activision Blizzard and the Future of Gaming*, *supra* note 47; Sarah E. Needleman & Aaron Tilley, *FTC's Tussle with Microsoft Puts the Spotlight on Cloud Gaming*, WALL ST. J. (Dec. 11, 2022, 7:53 PM), https://www.wsj.com/articles/battle-between-ftc-and-microsoft-turns-on-future-of-cloud-gaming-11670796726?mod=Searchresults_pos1&page=1 [https://perma.cc/A4BM-BRWG].

368 *See, e.g.*, Microsoft, 2023 WL 4443412, at *passim*; *FTC Complaint*, *supra* note 39, at *passim*; CMA, FINAL REPORT, *supra* note 54, at *passim*.

369 *Microsoft, Activision Blizzard and the Future of Gaming*, *supra* note 47.

370 *FTC Complaint*, *supra* note 39, at 9.

371 *Id.* at 17; CMA, FINAL REPORT, *supra* note 54, at *passim*.

372 CMA, FINAL REPORT, *supra* note 54, at 284–85, 294.

373 *Id.* at 294.

374 *See* discussion *supra* Section V.A.

375 FTC v. Microsoft Corp., No. 23-cv-02880-JSC, 2023 WL 4443412, at *13 (N.D. Cal. Jul. 10, 2023).

content, because the FTC's evidence focused on this one game."[376] Had the FTC introduced evidence on Activision's vast portfolio of other games, it may have been able to convince the court that Microsoft at least had an incentive to pursue a foreclosure strategy.[377]

As for cloud streaming, the court pointed to contractual obligations with five rival streaming companies, including Nintendo, to allow Activision content on their platforms for ten years.[378] Shortly after the court's decision and after rejecting Microsoft's offer for months, Sony also agreed to a ten-year contract for *Call of Duty*.[379] Sony's contract, however, only covers *Call of Duty*,[380] and the contracts with Nintendo and other streamers encompass more games, but the extent to which they will have access Microsoft's full portfolio is unclear.[381] The fact remains that Microsoft will be able to withhold every Activision game except *Call of Duty* from Sony and do the same for significant portions of Activision's portfolio from Nintendo and others. The CMA concluded that Microsoft would still benefit from a foreclosing only a portion of its games[382] and only approved the deal after Microsoft restructured it to exclude any possibility of foreclosing Activision's content in Europe.[383] That option remains largely open in the U.S.

The court found that because Activision currently withholds its games from any cloud streaming services, these contracts would expand access to Activision content by bringing its games to rival streamers for

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376 *Id.* at *18.

377 *See id.* ("While other games, such as Diablo, are certainly popular, the FTC did not offer evidence that if Call of Duty remains multiplatform in the console market, making Diablo or other Activision titles exclusive to Xbox would probably substantially lessen competition in that market.").

378 *Id.* at *20.

379 Tom Warren, *Sony Agrees to 10-Year Call of Duty Deal with Microsoft*, VERGE (July 16, 2023, 9:05 AM), https://www.theverge.com/2023/7/16/23792215/sony-microsoft-call-of-duty-cod-deal-signed [https://perma.cc/8F4L-HEKE].

380 *Id.*

381 Nintendo's deal appears to extend beyond *Call of Duty*. *See* Jon Porter, *Microsoft Signs Binding Call of Duty Deal with Nintendo Ahead of EU Activision Hearing*, VERGE (Feb. 21, 2023, 3:56 AM), https://www.theverge.com/2023/2/21/23608256/microsoft-nintendo-call-of-duty-agreement-legal-eu-hearing [https://perma.cc/M9FD-FZE7] (noting that the agreement includes other Activision games). And Nvidia's deal includes "Xbox PC games," which by definition excludes console only games. *See* Sean Hollister, *How Microsoft's Nvidia Deal Works for Gamers — with or Without Activision*, VERGE (Feb. 21, 2023, 3:02 PM), https://www.theverge.com/2023/2/21/23609133/nvidia-microsoft-activision-blizzard-geforce-now-cloud-gaming-interview [https://perma.cc/UEJ6-43KY] (noting deal only includes PC versions of games).

382 CMA, FINAL REPORT, *supra* note 54, at 294.

383 Foreclosure is impossible because Microsoft sold the streaming rights for all of Activision's content in Europe to Ubisoft. *See supra* notes 84–85 and accompanying text.

the first time.[384] Thus, it held "[t]he merger will enhance, not lessen, competition in the cloud-streaming market."[385] While this argument has some merit, it ignores the fact that at some point, Activision will be forced to offer its games on streaming services as the industry turns towards streaming and consumer demand evolves, just as competitors Electronic Arts and Ubisoft have done.[386] The CMA, which also considered these contracts, came to this exact conclusion in its evaluation of the merger,[387] but the FTC failed to offer any evidence supporting this fact nor did it model the cloud gaming market.[388]

Moreover, the procompetitive value of these contracts is suspect. Nintendo's Switch presently lacks the technological capability to play *Call of Duty*.[389] Further, a ten-year commitment to offer Activision content on rival platforms will be meaningless if those rivals do not exist by then. As discussed in the next Section, the cloud gaming market faces high barriers to entry, and even tech titans have already struggled or left the market entirely.[390]

Regardless, these contracts leave open an avenue for Microsoft to pursue an exclusivity strategy with Activision games. History indicates it will do so to bolster its nascent Game Pass.

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384 FTC v. Microsoft Corp., No. 23-cv-02880-JSC, 2023 WL 4443412, at *20 (N.D. Cal. Jul. 10, 2023).
385 *Id.*
386 Electronic Arts offers its subscription service EA Play on Xbox Game Pass. *Xbox Game Pass*, MICROSOFT, https://www.xbox.com/en-US/xbox-game-pass?ef_id=_k_Cj0KCQjwiIOmBhDjARIsAP6YhSU94wbrm5-9XcxFBC2GdDR4OwU6u0sFLXjin7qsZs8t0Htzlff8JRcaAuraEALw_wcB_k_&OCID=AIDcmmiixzwwab_SEM__k_Cj0KCQjwiIOmBhDjARIsAP6YhSU94wbrm5-9XcxFBC2GdDR4OwU6u0sFLXjin7qsZs8t0Htzlff8JRcaAuraEALw_wcB_k_&gad=1&gclid=Cj0KCQjwiIOmBhDjARIsAP6YhSU94wbrm5-9XcxFBC2GdDR4OwU6u0sFLXjin7qsZs8t0Htzlff8JRcaAuraEALw_wcB [https://perma.cc/4LFC-CMXJ]. Ubisoft offers its games on Xbox and Amazon Luna. *Ubisoft+*, Ubisoft Store, https://store.ubisoft.com/us/ubisoftplus [https://perma.cc/DCP8-2NXT].
387 CMA, FINAL REPORT, *supra* note 54, at 259–60 ("[W]e consider that Activision would likely have made its games – including day and date releases – available for cloud gaming in the next five years.").
388 *Microsoft*, 2023 WL 4443412, at *20.
389 CMA, FINAL REPORT, *supra* note 54, at 14 ("Nintendo does not currently offer [*Call of Duty*], and we have seen no evidence to suggest that its consoles would be technically capable of running a version of [*Call of Duty*] that is similar to those in Xbox and PlayStation in terms of quality of gameplay and content.").
390 *See* discussion *infra* Section V.B.3.

3. Exclusivity Harms Consumers and Exacerbates Barriers to Entry

Given Microsoft's ability and incentive to foreclose rivals, this Section examines the potential ramifications of foreclosure. It concludes that further exclusivity in video games would harm consumers and exacerbate already high barriers to entry. This analysis has ramifications for other platform vertical mergers.

Exclusive games inherently limit a consumer's choice. Courts have likened a material reduction in consumer choice to a deterioration in quality,[391] which is a recognized form of anticompetitive harm.[392] Most consumers only own one console.[393] When faced with a desire to play a game exclusive to a console they do not own, they either forego playing it and forfeit any potential utility or are forced to pay hundreds of dollars for an entirely new console. In the short term, consumers may be forced to switch to their second-choice console or purchase multiple to play desired games.[394] Accordingly, a material reduction in choice also has real implications on consumer costs. Empirical evidence has suggested that removing exclusivity in the early 2000s would have returned $1.5 billion of value to consumers.[395]

Some academic literature assumes that platforms have an inherently low barrier to entry due to the limited capital required to start a digital business.[396] These scholars suggest that as quickly as a firm can acquire dominance it can just as quickly be supplanted by a startup.[397] An early article on platform antitrust used video game consoles as an example of a digital industry free from entry barriers noting "successive entry by Magnavox (1972), Atari (1975), Coleco (1976), Fairchild (1976), Mattel (1979), Nintendo (1985), Sega (1989), Sony (1995), and Microsoft (2001)."[398] Yet, 20 years after that article was published, there has been no meaningful entrant to video game consoles since the Xbox in 2001.

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391 Jonathan M. Jacobson, *Exclusive Dealing, "Foreclosure," and Consumer Harm*, 70 ANTITRUST L.J. 311, 356 (2002) ("A material reduction in the choices available is no different in kind than a reduction in quality, and all agree that a deterioration in quality is a cognizable form of consumer harm.").

392 *See* discussion *infra* Section V.C.

393 Recent data suggests the percentage of dual console ownership is increasing. In 2021, around one third of US households owned both a PlayStation and an Xbox, up from about a quarter in 2019. Gardner, *supra* note 252.

394 The CMA estimated that the unavailability of *Call of Duty* alone would entice consumers to switch from PlayStation to Xbox. CMA, FINAL REPORT, *supra* note 54, at 145.

395 Lee, *supra* note 41, at 2962.

396 Khan, *supra* note 102, at 1078.

397 *Id.*

398 Evans, *supra* note 32, at 365.

Such commentary underestimates the enduring power of network effects. Once established, the gravitational pull of network effects can become irresistible, locking in consumers to a platform even if a newer competitor offers a technically superior product.[399] Further, while platforms often enjoy high margins once established, many platforms require an immense upfront investment.[400] Increasingly, the creation of platforms has depended on the accumulation of huge data sets which also requires immense capital investments.[401] Few firms possess the capital necessary to do so.

Video games exhibit these same characteristics both in the creation of the platform (consoles or now streaming services) and the creation of games themselves, which can cost millions of dollars to create or secure exclusively.[402] A new entrant in the console market is unlikely as the industry shifts towards streaming, and indeed all new entrants have only built game-subscription services.[403] While Microsoft has tried to minimize its position,[404] streaming is an area where the company has a demonstrated advantage. First, Xbox Game Pass already leads the market in both share and technology.[405] Unlike Nintendo and Sony, Microsoft operates its own cloud infrastructure business, providing further vertical integration and a significant advantage over existing incumbents.[406] Sony has already turned

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399 *See* Khan, *supra* note 102, at 1079 ("Bigger is generally better. But the same demand-side economies of scale that help a network form can also come to shield the network from competition, as a potential competitor must induce a significant number of users to choose its network over the existing good or service. In the absence of interconnection, the switching costs for users can be significant, making it difficult for even a rival with a superior product or service to induce users to switch.").

400 *Id.*

401 Khan notes the example of Google Maps which was

> built through collecting billions of user data inputs, operating camera-fitted cars that collected more than 21.5 billion megabytes of street-view images from around the world, and combining multiple sources of place data across various Android devices. Theoretically a new firm could attempt to build a rival service by relying on public data, but the continued data inputs that Google Maps receives after achieving initial success are likely to keep any potential competitor a distant second. *Id.*

402 CMA, FINAL REPORT, *supra* note 54, at 301–02.

403 *See* discussion *supra* Section II.C.

404 Referring to itself as "last place in console, seventh place in PC, and nowhere in mobile game distribution globally." ME/6983/22– Microsoft/Activision Blizzard Microsoft's Response to The CMA's Reference Decision at 4 (Oct. 11, 2022), https://assets.publishing.service.gov.uk/media/634e5d3dd3bf7f618d8f88d1/Activision_-_Initial_Phase_2_submission_a.pdf [https://perma.cc/4LAW-AU29].

405 CMA, FINAL REPORT, *supra* note 54, at 4, 8, 294.

406 Amazon, Microsoft, and Google lead the cloud computing infrastructure market, respectively. Jason Cohen, *4 Companies Control 67% of the World's Cloud Infrastructure*, PC

to Microsoft for help building its own game streaming service based on its Microsoft Azure.[407] The CMA considered Microsoft's cloud infrastructure an immense cost advantage over rivals who do not have one.[408] While Amazon and Google offer their own cloud infrastructure services and have built their own game streaming platforms, they lack both their own games or experience securing them.[409] Accordingly, Microsoft's unique combination of cloud infrastructure and established gaming catalog led the CMA to conclude the company has a cost advantage "that no cloud gaming rival can match" and that the market as a whole faces significant entry barriers.[410]

For evidence of preclusive entry barriers in this industry, look no further than Google. In 2019, *The Economist* predicted that Google's and Amazon's computing expertise and extensive data center resources could pose a serious threat to the Big 3's dominance as the industry transitions to streaming.[411] Yet in 2022, Google announced it would discontinue its Stadia game streaming service, less than three years after its launch.[412] Lack of access to exclusive gaming content, like those offered by rivals, could have been to blame. In 2019, Forbes well summarized Stadia's problem:

> Picking Stadia over Xbox or PlayStation or PC means you are foregoing access to all three pools of exclusives from Nintendo, Microsoft and Sony, as opposed to two of the three if you bought an actual console, given that Stadia does not have any exclusives of note of their own at this point.[413]

MAGAZINE (Dec. 29, 2021), https://www.pcmag.com/news/four-companies-control-67-of-the-worlds-cloud-infrastructure [https://perma.cc/35GG-36GL].

407 Vic Hood, *Sony is Working on a Cloud Gaming Strategy that Is 'Unique and Only on PlayStation'*, TECHRADAR (Apr. 22, 2021), https://www.techradar.com/news/sony-is-working-on-a-cloud-gaming-strategy-that-is-unique-and-only-on-playstation [https://perma.cc/4Z98-VBTQ].

408 CMA, FINAL REPORT, *supra* note 54, at 236–37.

409 *Id.* at 246–47.

410 *Id.* at 287.

411 *Netflix, but for Video Games*, *supra* note 87.

412 Tom Gerken, *Google to Close Stadia Cloud Service and Refund Gamers*, BBC (Sep. 29, 2022), https://www.bbc.com/news/technology-63082320 [https://perma.cc/XS77-9DZ9].

413 Paul Tassi, *Google Stadia Lacks Exclusives and Is Still Missing the Biggest Third-Party Games of the Year*, FORBES (Aug. 20, 2019, 8:03 AM), https://www.forbes.com/sites/paultassi/2019/08/20/google-stadia-lacks-exclusives-and-is-still-missing-the-biggest-third-party-games-of-the-year/?sh=35250201313e [https://perma.cc/EE7F-YXPC].

This problem endured, with commentators attributing Stadia's demise to a lack of exclusive AAA games.[414] One Google employee speculated that Stadia struggled to obtain exclusive titles because of the video game industry's recent consolidation and continued use of exclusive dealing by the Big 3.[415] Meanwhile, Amazon's Luna continues to struggle.[416]

Exclusive Activision content would only exacerbate high barriers to entry in this market. As a top game studio, Activision possesses a larger portfolio of games than most, and its content normally releases across multiple platforms.[417] Absent a merger, the CMA concluded that Activision content would likely appear across multiple streaming platforms.[418] Removing access to this important game portfolio would significantly impair the ability of other rivals to procure the gaming content necessary to establish critical mass and would therefore likely substantially lessen competition.[419]

C. *Non-Pricing Harms*

While for many decades antitrust analysis has focused on pricing impacts, U.S. antitrust law has long embraced other types of competitive harms. In *AT&T*, the court reminded readers that "[v]ertical mergers can create harms beyond higher prices for consumers, including decreased product quality and reduced innovation."[420] However, the DOJ did not argue non-pricing harms.[421] It is unclear whether any quality or innovation concerns were present for the AT&T-Time Warner merger, but the D.C. Circuit acknowledged that a merger challenge can succeed without showing

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[414] Kris Holt, *Google Reportedly Canceled a Stadia-Exclusive Follow-up to 'Death Stranding'*, ENGADGET (Oct. 1, 2022, 4:08 PM), https://www.engadget.com/google-stadia-death-stranding-follow-up-exclusive-report-200857092.html [https://perma.cc/9J4L-FZVK].

[415] Rebekah Valentine, *Stadia's Shutdown: The History of Google's Doomed Project, From Those Inside and Out*, IGN (Oct 7, 2022, 12:54 PM), https://www.ign.com/articles/stadias-shutdown-the-history-of-googles-doomed-project-from-those-inside-and-out [https://perma.cc/73G7-PYQQ]; *see also* CMA, FINAL REPORT, *supra* note 54, at 246.

[416] Sean Hollister, *Amid Layoffs and Lost Games, Amazon Luna Comes to Canada, Germany, and the UK*, VERGE (Mar. 22, 2023, 1:28 PM), https://www.theverge.com/2023/3/22/23651924/amazon-luna-expand-canada-germany-uk [https://perma.cc/6RXP-HJLC].

[417] Chris Scullion, *Microsoft Was Metacritic's Highest-Rated Publisher in 2021, With the Largest Average Score Ever*, VIDEO GAMES CHRON. (Mar. 9, 2022, 10:58 AM), https://www.videogameschronicle.com/news/microsoft-was-metacritics-highest-rated-publisher-in-2021-with-the-largest-average-score-ever/ [https://perma.cc/KM24-CVRV].

[418] CMA, FINAL REPORT, *supra* note 54, at 303.

[419] *Id.* at 303–04.

[420] United States v. AT&T, Inc., 916 F.3d 1029, 1045 (D.C. Cir. 2019).

[421] *Id.*

any quantitative price increases if the merger will likely reduce quality and innovation.[422] The FTC alleged that the Microsoft acquisition will adversely affect quality and innovation.[423] This Section explores the existing evidence for that argument.

Historically, mergers in the video game industry have improved quality. A previous Section discussed a Gil and Warzynski's study, which found that vertically integrated developers tend to produce improved quality games due to the combined firm's ability to coordinate.[424] A similar study in the UK confirms this phenomenon and finds mergers tend to increase the percentage of games receiving positive critical reviews.[425] However, this same study found that concentration among developers reduces the number of innovative games.[426] The authors explain that larger developers effectively identify independent studios that produce great games but fail to nurture their innovative capabilities post-merger.[427] In other words, merged firms are better at repeatedly developing the status quo but fail to produce novel content. Against Microsoft, the FTC made an innovation argument, but it was clear it faced an uphill battle to meet its burden.[428]

Alternatively, the FTC argued that the merger would diminish the quality of games on rival platforms.[429] The CMA has concluded that Microsoft could likely, as part of its foreclosure strategy, degrade the quality of Activision's games on rival platforms.[430] Microsoft could do this in several ways including inferior technical qualities (reduced graphics, latency, lower frames per second, longer load times), creating exclusive gaming content that is only available on Xbox, or timed exclusivity

422 *Id.* (citing Ford Motor Co. v. United States, 405 U.S. 562, 567–69 (1972)).

423 *FTC Complaint*, *supra* note 39, at 17.

424 *See* discussion *supra* Section V.A.

425 Masakazu Ishihara & Joost Rietveld, *The Effect of Acquisitions on Product Innovativeness, Quality, and Sales Performance: Evidence from the Console Video Game Industry (2002-2010)*, at 28 (NYU Working Paper, 2017), https://papers.ssrn.com/sol3/Delivery.cfm/SSRN_ID2897264_code857559.pdf?abstractid=2897264&mirid=1&type=2) [https://perma.cc/SGH3-VVRK]; *see also* Lee, *supra* note 41, at 2963 (finding "integrated software was higher quality than non-integrated and non-exclusive titles").

426 Ishihara & Rietveld, *supra* note 425, at 28.

427 One underlying explanation is that the creative personalities that produce innovative content tend to like working for smaller, unstructured, independent developers. *Id.*

428 FTC v. Microsoft Corp., No. 23-cv-02880-JSC, 2023 WL 4443412, at *17 (N.D. Cal. Jul. 10, 2023).

429 *Id.* at *18.

430 CMA, FINAL REPORT, *supra* note 54, at 160.

(releasing the game to other platforms at a later date).[431] However, the FTC failed to introduce expert testimony supporting any of these theories.[432]

In the long term, Microsoft's foreclosure strategy could significantly reduce competitive forces, thereby reducing the incentive to innovate or provide quality games in the future. This is true of other platforms also where long-term dominance reduces the incentive for new firms to invest in innovative ideas because the costs associated with entry are too high.[433]

VI. CONCLUSION

Current attitudes towards vertical mergers allow dominant firms to pursue anticompetitive conduct with little fear of recourse. The efficiency benefits of vertical mergers are overstated, and anticompetitive effects can and do arise post-merger. This Article showed that a platform like Microsoft's Xbox is more likely to pursue anticompetitive conduct through merger than traditional firms. While economists and antitrust experts typically hold that foreclosure is unlikely in vertical mergers, Microsoft has an incentive to foreclose rivals from Activision's content due to an inherent profit incentive stemming from network effects. Such conduct could raise rivals' costs and exacerbate already prohibitively high barriers to entry. This outcome in the largest entertainment industry in the world could devastate consumers.

Until the law deviates from the strong procompetitive assumptions on vertical mergers, digital platforms will continue to pursue problematic acquisitions unchecked. Some in Congress have called for updates to U.S. antitrust laws, which have stood largely unchanged since their original passing over 100 years ago.[434] The House's antitrust subcommittee has recommended a statutory presumption that vertical mergers by dominant firms in concentrated markets are anticompetitive.[435] Similarly, Senator Amy Klobuchar's proposed Competition and Antitrust Law Enforcement Reform Act provides for a presumption that exclusionary conduct creates an appreciable risk of harming competition

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431 *Id.* at 160–61.

432 *Microsoft*, 2023 WL 4443412, at *18.

433 Khan, *supra* note 102, at 1008–09.

434 McCabe & Lohr, *supra* note 134.

435 *See House Antitrust Report*, *supra* note 1, at 334 ("[T]he subcommittee recommends that Congress explore presumptions involving vertical mergers, such as a presumption that vertical mergers are anticompetitive when either of the merging parties is a dominant firm operating in a concentrated market, or presumptions relating to input foreclosure and customer foreclosure.").

if the firm has a market share of 50% or more or has significant market power.[436]

Default anticompetitive presumptions would undoubtedly put more mergers under scrutiny and reverse decades of chronic merger underenforcement. However, they may also risk swinging too far back towards merger overenforcement. Even though vertical mergers can result in harm, many do not. Overburdening companies that do not deserve intense scrutiny would result in unnecessary inefficiency. Some scholars have proposed a narrower anticompetitive assumption applying only to dominant platforms.[437] Given the relatively higher risk of anticompetitive conduct associated with platforms discussed in this Article, such a targeted rule makes sense. Once antitrust law hits the rest button on strong procompetitive vertical merger assumptions, the Agencies will be better equipped to challenge harmful mergers.

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436 Competition and Antitrust Law Enforcement Reform Act of 2021, S. 225, 117th Cong. § 9(c) (2021).

437 *See* Baker et al., *supra* note 159, at 16 (proposing a dominant platform presumption).