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Thou Shalt Not Commit Filicide: Antitrust's Make-or-Buy Problem Reinvigorated

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According to Wikipedia, the term "*filicide*" refers to a deliberate act of a parent killing their own child. As awful as that sounds, in corporate life it is pretty common for undertakings to divest, diminish, or discontinue entire product lines, services, distribution chains, or complementary divisions of work. This is often done as a response to a few antecedents, such as changing environmental conditions, ineffective market strategies, poor firm performance, inefficient governance, financial restructuring, perceived competitive advantages, or business transactions.

Yet recently, several deals attracted criticism, including through antitrust inquiries, for another reason. These challenges allege that acquirers seek to "*commit filicide*" by killing off their existing products/services after purchasing assets corresponding to similar lines of business. By pursuing these cases, the antitrust authorities seem to favour competition to be carried out via in-house production, rather than by purchasing an existing (or emerging) bundle of assets. In other words, antitrust authorities seem to prefer "firms that make", over "firms that buy", without caring much for alternative explanations or underlying business rationales. The aim of this piece is to figure out why this is so, and whether it is a sensible policy path to embark upon.

What is corporate filicide, and why do authorities care?

Recent examples of transactions arousing suspicion

In order to determine why regulators plan to set out a policy preference that favours in-house production over purchases of ready-made assets, it would be beneficial to first illustrate the topic by providing a few recent examples. After concretizing specific cases, we will proceed with searching for clues as to the potential motivations behind the efforts to move policy in such a direction. Lastly, we will highlight the methods, such as theories of harm, with which the agencies aspire to tackle these transactions.

One can think of three recent business transactions that fall under the *filicide* concept being developed here. [1]

First is the Amazon/One Medical deal. One Medical is a primary care service provider that is active in the telemedicine sector. As known, telemedicine has been a highly dynamic sector that experienced surging growth since the advent of the pandemic, with large players endeavouring to enter the market via acquisitions of their own. Amazon's move to acquire One Medical may be plausibly seen in this light; it can be interpreted as a response to the moligopolistic competition exerted by the likes of Google. Other possible explanations may be grounded upon the fact that it is very difficult to locate and recruit physicians, construct insurance networks, and build robust relationships with customers, such as employers.

The second deal is Meta's proposed acquisition of Within. Within develops a fitness app ("Supernatural") that is compatible with application stores in VR headsets, such as Oculus produced by Meta. Unlike its Facebook app, which is a standalone software product that needs hardware (a device like a smartphone) to run on, Oculus is a further step in integration that combines software and hardware, much like Apple iPhones and the App Store. So, there may be potential conflicts of interest at play here that can give rise to primary-line discrimination claims, in favour of Oculus.

The third and last deal is the recently announced intention of Adobe to purchase Figma. Both undertakings are active in the overall market for visual design software, with flagship products like Photoshop and Illustrator for Adobe, with Figma acting as a disrupting entrant for close to a decade. Commentators argue that Adobe is after the collaborative design platform to make up for the lacklustre performance of its own equivalent service, Adobe XD. Alternatively, the transaction may also be an attempt to bolster Adobe's prominence in the web-based user interface and user design software tools market, which is the primary strength of Figma products.

Why are regulators concerned?

As we alluded to with reference to Meta/Within deal, some of these transactions may prompt allegations of self-preferencing (or vertical foreclosure) should the offer manages to go through. Another explanation may point toward the rising "precautionary antitrust movement", for which the concept of "killer acquisitions" holds considerable weight.

Interestingly, neither of these motivations explains the phenomenon. For instance, within the context of FTC's investigation into the Meta/Within deal, the agency does not allege any infringement based on leveraging or discrimination claims. Killer acquisitions and the precautionary antitrust movement condemn the acquisition and subsequent discontinuation of nascent/emerging firms as anticompetitive. By contrast, the aforementioned cases entail the closure of in-house products/services after an acquisition has been made (hence the term "filicide"). It is filicide that has attracted the attention of commentators and government agencies. Aside from investigating Meta, the FTC initiated an inquiry to block Amazon's acquisition of One Medical, and similar calls to arms have been made as regards Adobe's decision to purchase Figma. The main argument is as follows: "*absent this transaction, Adobe/Amazon/Meta would continue to innovate via its own service, or enter into the target's market with a new product of its own*". [2]

The enmity towards corporate restructuring and the hostility towards corporate filicide can be explained by adherence to what some scholars called "the structuralist innovation presumption". Accordingly, antitrust authorities may perceive certain market structures (such as those in which several competitors are always present) as more conducive to innovativeness. Viewed through this lens, for innovation to prosper, it would make sense to block acquisitions aiming to simply relocate assets and resources by placing them under the umbrella of another (purchasing) firm. Instead, it would be much more preferable to have two (or three, or four) undertakings striving to manufacture their own, competing products.

The problem with this approach is that the relationship between innovation, market structure, and competition, although one of the most heavily studied areas of industrial organization economics, still fails to provide clear implications for policy. Whereas it may be possible that a more atomized market may deliver greater gains in innovation, the same can also hold true for concentrated markets. Since empirical evidence is inconclusive, it is unclear whether fundamental rights of undertakings, such as the right to establishment and property, should be constrained via what is supposed to be an exceptional mechanism.

Going after such filicide cases may also double as an effective vehicle to pursue a strategy of "regulation by threat". By signalling to undertakings that "making" is the preferred form of competition as opposed to "buying", antitrust authorities may induce spill-over effects on adjacent markets, which may be especially effective in highly entangled industries like digital platforms. Regulatory threats are not necessarily evil, and they can solve certain dilemmas facing regulators in some industries, such as telecommunications. For instance, a case study in the German telecoms market demonstrated that threats of regulation generate a "best of both worlds" outcome, with the absence of such threats linked to reduced investments or competition. However, the hypothesis rests heavily on price-based industries, and its effects on dynamic, digital industries, where products are often priced at zero (at least, monetarily speaking) are less clear. For example, when it comes to non-price results, such as the elimination of greenhouse gas emissions, regulatory threats were not successful. Thus, there is a risk that the innovative motivations of firms may be diminished as a result of these governmental initiatives.

Potential consequences, intended and unintended

The consequences of a confrontational approach toward corporate filicides should be analysed in a step-by-step fashion.

Firstly, it is not certain whether the government is better informed and able to decide whether in-house production of a service is more beneficial for society than purchasing a similar service or assets from the market. Often, theories of the firm suggest that a firm will only integrate (that is, produce within its own boundaries rather than contracting through the market) if the costs of doing so are lower than the costs of operating the market system (transaction costs). In such scenarios, firms are better able to manage and coordinate the complexity of their operations from within their boundaries. There is a wide swath of literature on this topic, which eventually ties to the knowledge problem espoused by the Austrian school of economics.

It follows from the first point that, when firms decide to pursue transactions like acquisitions, they most likely have completed detailed market analyses and feasibility studies, the results of which plausibly point towards the potential efficiencies of an acquisition as opposed to in-house production. As with the cases analysed in this piece, forcing these firms to produce competing services in-house by prohibiting these transactions under merger laws would mean that, if at all, the acquirers will have to invest more resources to enter the market.

Assuming that firms indeed do so, their troubles will not cease. As exemplified both by recent case law and legislative developments, these firms (who are likely to be found dominant or a "gatekeeper") will also be unable to "self-preference". In plain terms, they are forced to undertake costlier investments, while simultaneously, if and once they create in-house equivalents, they are prohibited from taking action to help recoup their (heightened) expenses. Regulators would at once expect companies to be subject to an inefficient allocation of resources, and when they self-preference, argue that they are not as efficient as their competitors, because otherwise, they would not have needed to engage in self-preferencing.

Compounding the above analysis is the fact that the prohibitions would act as a double barrier to exit, or a deterrent to divestiture. When a transaction, like the ones examined here, is proposed, the motivation is such that both the acquirer and the target wish to exit the market. The acquirer would cease its (inefficient) in-house production and take hold of the target's (superior) operations. Blocking such transactions for the sake of forcing undertakings to manufacture in-house would act as a barrier to exit for both firms – and we know that barriers to exit are, in reality, barriers to entry.

Conclusions

The recent calls to rein in corporate filicide, that is, forcing firms to manufacture in-house equivalents of products they wish to acquire, stem from an adherence to specific market structures deemed ideal for innovative growth. Not only is this approach empirically unjustified, but it is also fraught with problems from a theoretical perspective.

Antitrust and regulatory agencies trying to block acquisitions in order to force firms to "make rather than buy" effectively forgo a market-induced scenario to the benefit of a (supposedly) better alternative they envisioned. It is true that uncertainty is prevalent in all parts of governmental and economic activity. Even naked price-fixing cartels may at times increase economic efficiency – but agencies often prohibit those in a *per se* fashion, and for good reason – uncertainty regarding their effects rarely materializes heavily enough to justify collusion. By contrast, directly intervening in the market for corporate control in dynamic industries, where no agency or person can know if the forgone alternatives might have produced more growth or innovation, is fraught with dangers. The task of compiling and correctly analysing the relevant information necessary to navigate these contingencies becomes more and more arduous as dynamism increases in a market. Thus, at least in dynamic industries, such as telemedicine, computer software, and virtual reality, it would be much more sensible to entrust the market process by separating the wheat from the chaff.

There may be countless reasons behind a firm's decision to produce in-house or purchase another firm's existing assets. As discussed, there may also be many antecedents informing a decision to divest or discontinue a line of business. Second-guessing these decisions and forcing firms to produce in-house when it is inefficient for them to do so risks economic damage and perverse incentives. Combined with the recent calls to introduce bans on self-preferencing, attacking corporate filicide leaves little for undertakings to work within an environment as hostile as it is dynamic.

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[1] US FTC's purported investigation into Amazon's purchase of iRobot may also qualify. The

report by Politico outlines that Amazon has a competing product ("Astro") that is an inferior device compared to what iRobot manufactures, which may potentially signal that Amazon may be willing to discontinue the development of its in-house gadget, committing corporate filicide. However, as details are scarce vis-à-vis that transaction, it has been left out.

[2] Even though recently reinvigorated, this is not entirely a new phenomenon. For example, in 1993, the US Department of Justice filed suit against the proposed deal between *Allison Transmissions/ZF*. One of the alleged theories of harm depended on Allison's potential to continue competing with ZF through its in-house heavy truck transmission products. Although the parameters of this case are unique (especially with regard to the concentration levels of the relevant market), the alleged theory of harm is very similar to what we have recently been seeing.

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