Opinion by Former Senior Government Officials and Leading Antitrust Experts on the Significant Antitrust Risks Posed by Broadcom's proposed takeover of Qualcomm

Abstract:

There are material regulatory risks associated with any combination of Broadcom and Qualcomm. Given the parties' competitive positions in WiFi and RFFE products (among others), the complexity of complying with a divestiture demand because of the difficulty the parties will have separating these businesses and selling them to an acceptable buyer, and the real risk that agencies (e.g., China's MOFCOM) may demand significant restrictions on Broadcom's post-merger licensing and distribution practices, the transaction presents significant antitrust risk.

Based on our experience as former senior government officials and practitioners with significant cross-border antitrust merger review experience, we write to share the significant antitrust risks posed by Broadcom's proposed takeover of Qualcomm.[1]

Broadcom's February 9, 2018 proposed merger agreement states, in relevant part, that: (1) Broadcom agrees to use its "reasonable best efforts" to complete the process; (2) to that end, it is willing to divest Qualcomm's network (but not mobile) WiFi and Radio Frequency Front-End (RFFE) assets or businesses (excluding integrated products such as Snapdragon) and any other Qualcomm assets, licenses, or other businesses so long as not material; and (3) Broadcom will pay Qualcomm a reverse break-up fee of $8 billion in the event that regulatory approval is not received, assuming that there has been no "material adverse effects" (MAEs) on Qualcomm's businesses.

The proposed agreement further provides for the following limitations on Qualcomm during the period between signing and closing: (1) prohibitions on initiating litigation, including to enforce its intellectual property rights (IPRs) against infringers who refuse to pay; (2) prohibitions on entering into any license agreement or materially amending existing agreements; and (3) prohibitions on settling existing litigation without Broadcom's consent. Based on public reports, we also understand that Broadcom has further stated that it is now willing to commit to additional divestitures, including its own connectivity businesses, but has not agreed to commit to accept conduct remedies such as prohibitions on bundling or tying products.[2]

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[1] Some of the signatories are affiliated with U.S.-based law firms that represent Qualcomm in policy or other matters. Professor Hwang Lee served as an expert for Qualcomm in unrelated Korea Fair Trade Commission matters.

[2] According to press: "In the meeting this week, Singapore-based Broadcom was willing to make certain divestitures to satisfy antitrust regulators, but was still resistant to 'other commitments that could be expected' to be required by government regulatory bodies, Qualcomm said." Greg Roumeliotis & Diane Bartz, *Qualcomm Says Open to More Deal Talks With Broadcom Following Meeting*, US NEWS (Feb. 16, 2018, 8:21 am), https://money.usnews.com/investing/news/articles/2018-02-16/qualcomm-says-open-to-talks-with-broadcom-for-better-offer. However, in its filing to the SEC yesterday, Broadcom reiterated its willingness to accept only those limited divestitures set forth in its original proposed merger agreement. Qualcomm Incorporated, Proxy Statement (filed by Broadcom Limited) (Schedule 14A Information) (Feb. 20, 2018).

Given these terms, shareholders should be aware of the following:

(1) the real risk that foreign antitrust agencies will impose onerous remedies that either restrict the parties' ability to engage in certain conduct or require them to take specific actions;

(2) the prior actions of antitrust agencies in rejecting proposed divestiture buyers that do not have both the ability and incentive to compete with the combined entity on day 1 and to take the technologies to the next generation;

(3) that similar complex cross-border deals have taken 18+ months to gain regulatory approval, especially where—as here—approval is required by numerous jurisdictions (here, the United States, the European Union, China, India, Korea, and Taiwan); and

(4) the likelihood that Broadcom's proposed limitations on how Qualcomm can run its business from signing to close violate antitrust "gun-jumping" rules, which alone could be the subject of a separate investigation by the U.S. Federal Trade Commission and others.

With respect to conduct remedies, there are countless examples showing that regulators can and do impose substantial conduct remedies, including those that could amount to an MAE, and that may not be merger-specific. These include:

- Interoperability requirements (e.g., the European Commission's (EC's) Intel/McAfee and Intel/Altera decisions requiring the companies to take specific steps to ensure that their products interoperated with competitors' products);

- Prohibitions on tying or bundling products (e.g., the EC's Intel/McAfee and China's Ministry of Commerce's Merck/AZ);

- Prohibitions on seeking or enforcing injunctive relief on FRAND-assured SEPs (e.g., MOFCOM's Microsoft-Nokia);

- Price caps (e.g., MOFCOM's Microsoft-Nokia and Merck-AZ imposing royalty caps on IPRs);

- Requirements to invest in specific amounts of research and development (e.g., MOFCOM's Samsung/Seagate, requiring Seagate to invest at least $800 million a year for three years in innovation to ensure that the company would bring more innovative products and solutions to consumers);

- Non-merger-specific remedies to address other concerns the agencies may have already or discover during the review process (e.g., distribution-related remedies imposed by MOFCOM in ABI-SABMiller); and

- Other non-merger specific remedies to protect domestic champions (e.g., in *Google/Motorola*, MOFCOM required Google to maintain Android as open and to continue to provide Android to Chinese manufacturers on an expeditious basis).

The real risk posed by these types of remedies generally requires deal protection for shareholders, including a "hell-or-high-water clause" (i.e., do whatever is necessary to get the deal done), or at least defining the MAE provision so as to exclude remedies that may be required by antitrust regulators. Such protections ensure that a buyer cannot walk away from the deal at any point during or after a protracted regulatory review period, particularly given the likely disruption caused to targets (here, Qualcomm) during such a review period.

With respect to divestitures, antitrust agencies will require that any divestiture remedies fully replace the loss of Qualcomm's competitive pressure in the market, i.e., any remedy must make competition "whole" in the sense that it must put another competitor in a position to compete as effectively against Broadcom as Qualcomm does today (and likely into the future). And, of course, any divestiture transaction would itself have to be reviewed for antitrust and national security issues.

Prior agency precedent makes it clear that agencies require divestiture buyers have the incentive and ability to compete immediately, and continue competing into the future.

- *Applied Materials/Tokyo Electron* (2015) was abandoned after the U.S. Department of Justice (DOJ) rejected the parties' tool-line (product) divestitures as insufficient to preserve existing competition with respect to "the development of equipment for next-generation semiconductors" on the grounds that proposed <u>buyer was not already focused on the product-line</u> and did not have the same capacity to innovate. The DOJ was also concerned that the transaction would have combined "the two largest competitors with the necessary know-how, resources and ability to develop and supply" the technology products at issue.

- As DOJ's then Chief Economist observed, "[n]aturally, the Antitrust Division would be . . . wary of the ability of any remedy to replicate [the] competitive dynamic" and DOJ ultimately concluded "that replicating the competitive significance of one of the most innovative companies in a sector that is virtually synonymous with innovation would be exceptionally challenging."[3]

- The U.S. antitrust agencies have also rejected proposed divestiture buyers because they could not effectively compete on Day 1. *In Sysco Corp./US Foods Inc.*, the FTC rejected divestiture of facilities and sued to block the transaction; in *Staples Inc./Office Depot Inc.,* the FTC rejected divestiture of significant contracts, and sued to block the transaction; and in *Baker Hughes/Haliburton*, the DOJ rejected divestiture package because, among other things, the discreet assets were insufficient for remedy.

[3] Nicholas Hill, Nancy L. Rose, & Tor Winston, *Economics at the Antitrust Division 2014-2015: Comcast/Time Warner Cable and Applied Materials/Tokyo Electron*, 46 REV. IND. ORGAN. 425, 432 (2015), https://economics.mit.edu/files/12988.

With respect to likely review timing, recent deals suggest that the regulatory approval process is likely to take 18+ months (see e.g., Qualcomm/NXP—15+ months and counting despite the lack of direct competition between the parties; Penn State Hershey/Pinnacle—abandoned by the parties in 2016 after a 28 month review period; Advocacy Health Care/NorthShore University Health System—abandoned in 2017 after a 30 month review period; Halliburton/Baker Hughes—abandoned in 2016 after a 19 month review period; DuPont/Dow Chemical and Abbott Laboratories/Alere—each taking 20 months to gain necessary approvals. Indeed, the recent proposed merger of the #1 and #3 global suppliers of semiconductor manufacturing equipment was abandoned after an 18-month review period.

In short, there are material regulatory risks associated with any combination of Broadcom and Qualcomm. In the United States, Europe, and China, in particular, this deal raises significant issues that will require a substantial amount of time and effort for global regulatory agencies to resolve. Given the parties' competitive positions in WiFi and RFFE products (among others), the complexity of complying with a divestiture demand because of the difficulty the parties will have separating these businesses and selling them to an acceptable buyer, and the real risk that agencies (e.g., MOFCOM) may demand significant restrictions on Broadcom's post-merger licensing and distribution practices, the transaction presents significant antitrust risk.

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