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## CLIENT UPDATE



### The Israeli Competition Authority's Position regarding Digital Markets and the Israeli Digital Ecosystem

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Recently the Israeli Competition Authority ("ICA") has been engaged in various activities with regards to digital markets and the Israeli digital ecosystem. As these activities will affect the future of startups and the tech giants in their activities in Israel, we set forth below the main activities of the ICA.

The ICA published a report regarding an inquiry it performed concerning investments by the tech giants in Israeli startups and whether those could be considered as "Killer Acquisitions". The bottom line of the ICA's inquiry is that no indications were found that the reviewed transactions could be considered Killer Acquisitions.

The theory of harm of Killer Acquisitions considers acquisitions of a nascent firm, which aims to terminate the development of the acquired product (or potential product), remove it from the market and preempt future competition for the purchaser. This theory is being discussed around the world, *inter alia*, due to the larger discussion on the power gained in recent years by the tech giants (mainly Google, Apple, Facebook, Amazon and Microsoft).

The ICA's inquiry included review of 21 merger transactions between the tech giants and Israeli startups in digital markets, which were filed for its review during 2014-2019. The ICA requested post-integration detailed information from these companies as regards the relevant activities that were purchased and the rationale for these purchases. In addition, the ICA spoke to relevant participants in those markets, such as various investors and founders of such startups. The ICA found that in the small sample examined, no transaction led to the elimination of the acquired product from the target market, nor did any of the transactions led to the termination of a potential development by the target into a complementary market.

This inquiry was based on an earlier related publication by the ICA, where it discussed a suggested model for the analysis of startup acquisitions in digital markets. This model tries to categorize in an early stage of the review process which transactions may raise competitive concerns.

In this previous publication, the ICA noted that in the last decade, Israeli high-tech has grown rapidly. In 2019, there were approximately 121 M&A transactions involving Israeli companies with a total value of \$12.4 billion. Many of these deals were in digital markets. According to the ICA, these markets are often characterized by significant advantages to size and scope, and many of them have significant network effects. These characteristics suggest, according to the ICA, that digital markets tend to suffer from high barriers to entry and therefore, entities operating in these markets and not threatened by immediate competition, may try to maintain (or increase) their market dominance through mergers and acquisitions. In addition, the ICA considers that more emerging competition issues regarding conglomerate mergers (mergers between non-competing entities that are not active on different levels of the same supply chain) should be treated with particular caution, especially in digital markets (as opposed to other markets).

Therefore, the ICA suggested a basic model, which classifies mergers in digital markets into two categories: "green" and "yellow". Transactions classified as "green" are identified as transactions that are not expected to require a different competitive examination from that practiced in ordinary commercial markets; Transactions classified as "yellow" are identified as those in which additional competitive concerns relevant specifically to digital markets may arise and need to be further examined. The classification is based on the characteristics of the product purchased and the main motivations of the buyer for the purchase. For the benefit of the model, the ICA defined two types of products / services: interface products/services and stand-alone products/services. Interface products, according to the ICA, are products that are developed as complementary products based on a specific platform in order to improve or expand the platform's functionality, whereas standalone products are those that operate independently from other products or platforms. Furthermore, the ICA identified three main motivations for an acquisition: acqui-hire (recruitment of highly qualified employees); technology; and data and information. The purpose of the model, according to the ICA, is to provide a simple, effective and relatively quick tool for the initial identification of acquisitions that require a more in-depth examination, compared to those that are not likely to raise different competitive concerns than those examined in a traditional merger examination.

It will be interesting to see if and how this model will be used by the ICA in the future and whether it may affect its review process of mergers in digital markets, which will be filed for the ICA's approval, especially after the recent report that demonstrated no competitive harm in the transactions reviewed ex post by the ICA.. In addition, the ICA left some questions for future discussion, specifically whether the review process of such transactions in digital markets should take into account: competition on a one-stop-shop market in which incumbents compete on a product or service portfolio provided to business consumers; competition between large eco-systems; or maybe just competition in the startups' product markets?

In addition, in a panel held by the Haifa University regarding the regulation of the Internet giants, Michal Halperin, head of the ICA, stated that the ICA's main focus with regards to digital markets will be through legislation rather than enforcement, since according to the ICA, Israel is lagging behind the EU in this regard. To that end, Halperin mentioned that the ICA, together with the Consumer Protection Agency and the Privacy Agency are currently promoting legislation, which will handle the regulation of privacy and competition related matters to the benefit of consumers. According to Halperin, this suggested legislation will be similar to the GDPR rules and the California laws concerning privacy issues, with the relevant adjustments to the Israeli economy. Additionally, the ICA is working on legislation relating to platform to business interface, the aim of which is to help small businesses in their interactions with the tech giants, which will be similar to an EU directive on this issue. Aside from the stated legislation, Halperin explained that their main focus will be the effect of the tech giants' activity on Israeli consumers and businesses. To that end, Halperin stated that if there are any behavioral rules applied to the tech giants outside Israel, whether due to enforcement action or based on the companies' own initiative, the ICA will use it as a benchmark to the behavior of those companies in Israel. Lastly, Halperin stated that if there are Israeli specific aspects to a global merger, the ICA will not hesitate to continue examining such mergers, regardless of whether those were approved by foreign antitrust agencies.

Please find [here](#) the ICA's recent report with the conclusions on its inquiry (in English).

For the ICA's earlier report (in English), click [here](#).

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